ANNUAL REPORT 2011

Building a better picture for Main Street, one piece at a time.

Lyons Bancorp, Inc.
It's all about people.

PROFILE

Lyons Bancorp, Inc. is a bank holding company headquartered in Lyons, New York, with assets of $555.5 million at December 31, 2011. Lyons Bancorp, Inc. has one banking subsidiary, The Lyons National Bank.

The Lyons National Bank is a community bank with offices in Clyde, Lyons, Macedon, Newark, Ontario and Wolcott in Wayne County, Jordan in Onondaga County, Geneva in Ontario County, Penn Yan in Yates County and our newest office in Seneca County. The Lyons National Bank has one subsidiary, Lyons Realty Associates Corp.

ANNUAL MEETING

The annual meeting of the stockholders will take place at 4:30 p.m. on May 23, 2012 at the historic Ohmann Theatre in Lyons, New York.

STOCK SYMBOL

LYBC

TABLE OF CONTENTS

CELEBRATING THE RETIREMENT OF A LOYAL BOARD MEMBER AND DEAR FRIEND

In early 2011 our dear friend, loyal advisor and devoted Board Member, Ted Marshall, announced his decision to retire from his position as Board Member of Lyons Bancorp, Inc. Although we were saddened by his decision, we are appreciative to have had such an outstanding business associate and member of the community serve with us.

Ted joined the Board in December of 1994. During his tenure, Ted helped guide the Bank on its growth path, starting with a $68 million Bank with three offices to one that now has 11 offices and over $550 million in assets. His involvement in the community exemplifies his connection and dedication to the region.

Ted is the past President and CEO of E & V Energy Company and Marshall Brothers, Inc., President of Patriot Tank Lines, Inc., and President of Pyrus Energy, Inc. Ted is an active member of the community. He served on the Weedsport Village Board and was acting mayor for two years, and is a past director of the Port Bay Improvement Association. He is a member of the First Presbyterian Church of Weedsport and is an exempt member of the Weedsport Volunteer Fire Department. Ted lives in Weedsport with his wife Nancy. He has three grown children; James, Case, and Dorothy, and five grandchildren.

Ted's retirement is a bittersweet moment for the bank. We will miss his charisma, enthusiasm and his business acumen. Please join us in wishing Ted and his family the best and warmest wishes for their future.

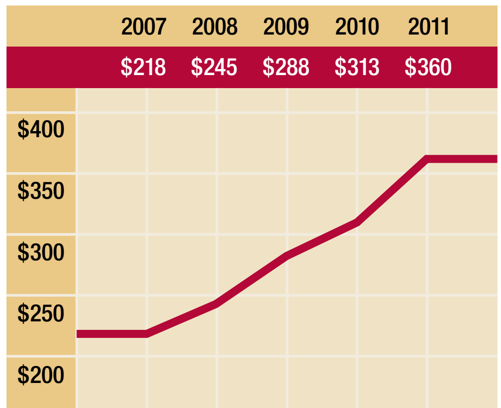
2011 IN RETROSPECT...

I began my message in our 2008 Annual Report by stating; "In keeping with the theme of change that has swept over America, we modified the format…of our annual report." From the feedback I received, that change was well received and we continue to use it. We also continue to be challenged with the "wave (sometimes it feels like a tsunami) of change" that I alluded to in my statement. These challenges have manifested themselves in the form of additional regulation, historically low levels of interest rates, and large bank restructuring. Before I get into those issues, there are many 2011 highlights I would like to share.

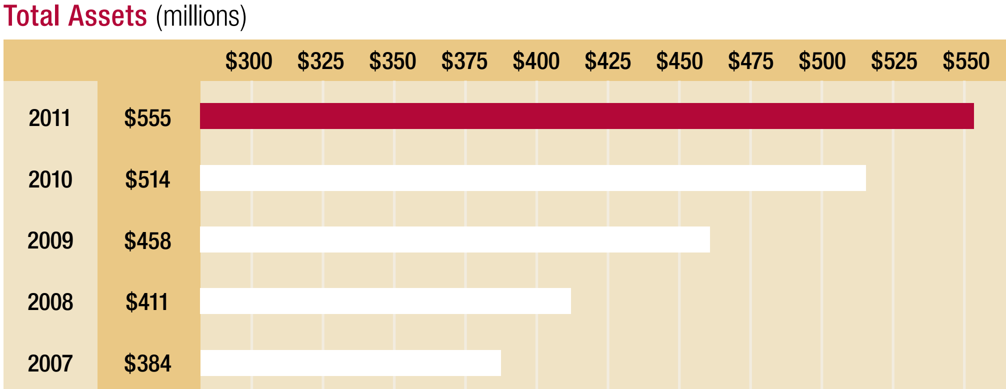
2011 RESULTS

I am pleased to report that, as much as the banking environment changes, there are constants. At LNB these constants are record earnings in 2011; business growth and increased market share; and the continued focus, dedication and professionalism of our employees. In 2011, our earnings per share on a fully diluted basis were $3.76. This is a 16% increase over the $3.24 per share we reported in 2010. In dollar terms, we earned $5.138 million versus the $4.168 million we booked the year before. From a balance sheet perspective, our assets at yearend totaled $555.5 million, as compared to yearend 2010 of $513.6 million, or an 8% increase. We grew every segment of our loan portfolio, resulting in an overall increase in loans of more than 15%. We originated 1,077 new residential mortgages in 2011 totaling over $94 million. We kept some of these mortgages on our balance sheet, and sold the balance. As we have done in the past, we continue to service (i.e. collect monthly payments, manage escrow balances) the vast majority of the mortgages we sell, which in turn, provides our customers with an accessible local contact in case an issue should arise.

Total Gross Loans (millions)

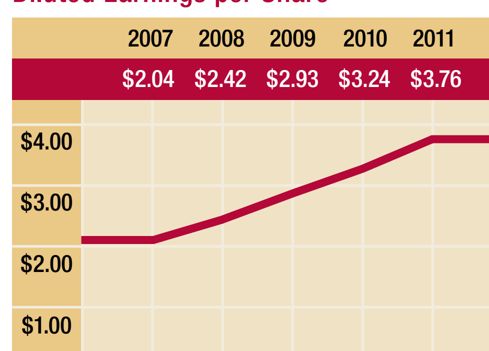


Total Assets (millions)



Robert A. Schick
President & Chief Executive Officer Lyons Bancorp, Inc., and The Lyons National Bank

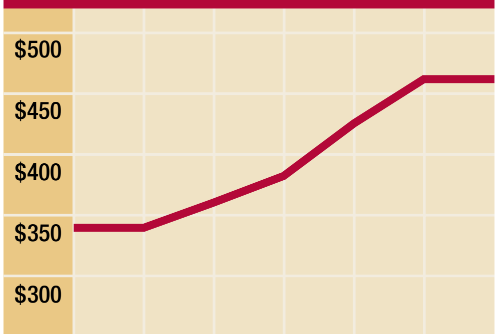
Diluted Earnings per Share



Bob Schick, *President & CEO* presents the **President's Employee of the Year Award** to Josh Miller, *Mortgage Underwriter*.

Total Deposits (millions)

	2007	2008	2009	2010	2011
	$343	$357	$382	$424	$461

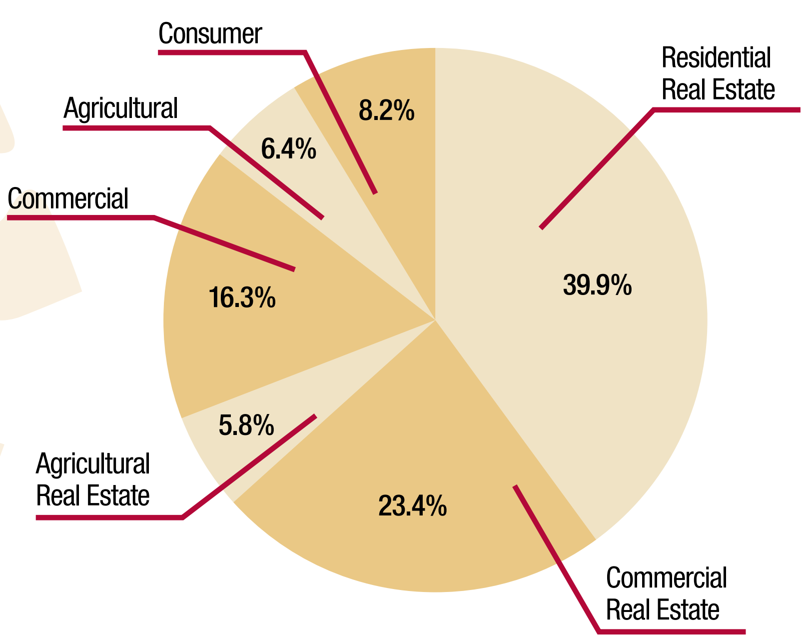


We again increased our deposit share in each of our branch markets. This boosted our deposit base by almost 9%. In January 2011, we opened our new branch facility in Seneca County, and have been very successful in gaining market share there. According to the June 30, 2011 Federal Deposit Insurance Corporation (FDIC) Deposit Market Share Report, our office is already the fourth largest branch bank in Seneca County. Kudos to Jill Hansen and her staff for achieving this level of success in a short period of time.

By design, we shrunk our investment portfolio by almost 5% and used the cash from maturing investments to fund higher yielding loans.

We added four new positions in 2011. New sales positions in our branch network and Financial Services Department will help drive revenue, and by adding staff in consumer and commercial loan operations departments, we increased our capacity to support the new business. Our annual payroll at December 31st totaled $6.8 million.

Loan Diversification



John J. Patrillo
"Our Beloved Friend and Associate"

On a very sad note, last spring we lost our dear friend and colleague, John Patrillo. John was a commercial loan officer who serviced our Seneca County market. We mourn his untimely passing and will keep him, his wife Sharon, their children and grandchildren in our prayers.

As December 2011 drew to a close, we opened our newly expanded space in Geneva. It houses executive offices and a technological state-of-the-art board and conference room. This new facility affords us the ability to participate in worldwide video conferencing and telecommunications and avoid the time lost to and expense of traveling. It is our intention to install a scaled-down version (due to limited space) of this technology in our Main Office in Lyons in early 2012.

Speaking of our Main Office in Lyons, we are giving the "grand old lady" a facelift. Built in 1929, the building needed extensive rehabilitation. Together with the technological upgrades I mentioned above, we have already replaced the famed arch windows and drapery, re-pointed much of the soffit, replaced the front doors and stoop, and re-wired the entire building. Moreover, due to the extensive work we did on our building, the Village of Lyons applied for and received a $500,000 "Main

Street Grant." Money from the grant will be used to rehabilitate other buildings in downtown Lyons. The pride we have in and the commitment we made to our Main Office is yet another example of what distinguishes a hometown bank from an out-of-area headquartered regional bank.

Finally, for the 27th time in the last 11 years, the Board of Directors showed its confidence in the Bank's ability to sustain its earnings growth, by again increasing the quarterly dividend. This January, I sent you a report from SNL Financial that depicted the growth in our dividend over the last 10 years. That growth at 411% ranks us second among banks in the entire country. This recognition, together with the recognition we received earlier last year regarding our ranking among the elite banks in the country when measuring return on average equity, is further testimony to the exceptional performance of our staff. While the buildings we build, the technology we install and the products we offer help us achieve the level of success we currently enjoy, it is the effort of our staff that pulls it all together. Their drive, diligence and commitment to be the best are what form our culture; and it is our culture that distinguishes us from the rest.

Our Challenges and what lies ahead…

I was recently asked by an industry colleague what keeps me awake at night. After not too long a pause, I replied that while change is inevitable and we at LNB have adapted to it successfully in the past, the severity and degree of change facing our industry has moved to an entirely new level. It will command our full attention. I added that some of the changes will be beneficial to our segment of the industry, but we will need to be at the top of our game to take full advantage of them. The examples I stated in my opening paragraph are foremost in my mind.

Suffice to say one would have to be totally naïve not to expect regulatory change from the events that caused the financial meltdown of 2008. But there is a vast difference between focusing specific legislation on the causes of the meltdown and those that took far too many liberties, and on the other hand, enacting broad based legislation. What resulted unfortunately was broad based–the Dodd-Frank Act. It paints the entire banking industry with the same brush. This legislation will have very severe unintended consequences on a segment of the industry–hometown banking–that the very legislators who voted for the Act admit was not culpable. To be fair, in some aspects, the Act does carve out smaller banks from compliance. However, history shows that market forces and regulatory best practice guidelines often trump these "carve outs."

The Dodd-Frank Act of 2010, in its original form, is 2,319 pages long and is a prime example of overkill (by comparison, the US Constitution, the law of the land, including the Bill of Rights, is 6 pages long). The Act covers an array of topics such as higher levels of required capital, creation of yet another consumer protection agency, heightened risk retention related to mortgages, permissible levels of fees banks charge for particular services, and many more. The last two mentioned, risk retention related to mortgages and permissible levels of fees are, in my estimation, most troubling.

People's Choice Award Recipients
Julie Smith, *Senior Teller;* Jennifer Smith, *Mortgage / Home Equity Processor;* Tara Rago, *AVP / Branch Manager;* and Dawn Shipman, *CSR.*

The People's Choice Award is awarded to an individual who provides exceptional customer service, emphasizes brand spirit, is a team player, shows consistency in performance and results, implements useful ideas for CRM management and portrays The WOW! Factor.

The risk retention issue affecting mortgages is known as "Qualified Mortgage" in Dodd-Frank. It essentially imposes broad risk retention requirements on most mortgages sold into the secondary market by requiring lenders to show the borrower has the ability to meet a repayment test. That in itself is not an issue. We don't make mortgages to individuals who don't show the ability to repay. The concern here is in the interpretation. As you know, residential mortgages can be for terms as long as 30 years. If this requirement test is deemed in a court of law to endure throughout the life of the loan, the long-term uncertainty will cause banks to either be more selective at the point of origination or the cost of the mortgage, i.e., the interest rate, will be adjusted to reflect the risk–or both.

How does this challenge LNB? We are a very active mortgage originator. Mortgages make up a fairly large segment of our business. I pointed out earlier that we originated over 1,000 mortgages in 2011, totaling more than $94 million. Currently, we hold almost $92 million in residential mortgages on our balance sheet and service another $130 million off-balance sheet. We earn interest income from these mortgages, generate fee income from the sale and servicing of mortgages and equally as important, sell other banking products, such as checking and savings accounts, car loans etc. to many of our mortgage customers. With all this activity, at yearend 2011 we had only three mortgages that were classified as non-accruing totaling $197,000. I believe our numbers prove we understand the mortgage market, know our customers well, and recognize how much room we have to operate within a "grey world." Then along comes legislation like Dodd-Frank that attempts to regulate everyone into a "black and white" environment. In such an environment both the Bank and our customers stand to lose. Another section of Dodd-Frank that has me concerned is the section that requires the Federal Reserve to regulate the amount of debit interchange fees banks can charge. This is a fee banks charge when merchants access the payment system to process your debit card purchase. My concern is that it directly inserts the government into a price-fixing role and is a dangerous precedent. In our free market society value-added and competition set prices, not the government. I wonder if one of the Washington Czars is preoccupied with the price of an oil change.

There are many more new regulations that have been bestowed upon us that I could enumerate, but space is limited. The point is the administration and compliance costs of these regulations continue to mount. An unintended consequence is further consolidation of the banking industry as smaller banks exit the market rather than struggle with these costs. Wasn't "too big to fail" at the heart of the meltdown?

The historically low levels of interest rates and the unlikely prospect that they will increase any time soon is just as challenging as is overbearing regulation. The majority of income generated by hometown banks like LNB is net interest income, which is the difference between the interest we earn on loans and investments and the interest we pay on deposits and borrowings. With an anemic economy driving interest rates to these lows, this differential is compressed. To offset the compression, banks need to efficiently increase volume and market share–hence our growth strategy.

Playing into our strategy is the fact that many of the larger banks, for various reasons, are shedding assets or abandoning the markets in which we operate. In 2012, we will become even more aggressive in capturing additional market share as these banks take their leave. We believe their exodus is a transformational opportunity for us. We also believe we have put ourselves in a position to take advantage of this opportunity because of our past commitment to assemble talented individuals and put in place advanced technology. But more needs to be done. Over the course of the next few years, we will seek out additional talent and evaluate even more advanced systems.

Additional facilities may be needed and further upgrades made to current ones. Be assured we will remain attentive to the short-term price we may need to pay for this long-term growth and plan diligently to recoup that cost as soon as possible.

In conclusion, as we work through 2012 and beyond, the wave of change and challenges that flow with it will again be formidable, causing our anxiety and frustration levels to rise. But as was the case in the past, the strong foundation we have built of talented individuals and advanced systems will allow us to prevail and get ready for the proverbial next wave.

Robert A. Schick
President & Chief Executive Officer
Lyons Bancorp, Inc. & The Lyons National Bank

VanAcker Farms, Williamson, NY
Scott MacKenzie, *LNB Commercial & Ag Loan Officer* (far right) pictured here with Dan and Lori VanAcker, LNB Customers and Owners of VanAcker Farms in Williamson, NY.

New Energy Works & Pioneer Mill
Jim King, *LNB Commercial Loan Officer* (left) pictured here with Jonathan Orpin, LNB Customer and Owner of New Energy Works & Pioneer Mill Works in Farmington, NY.

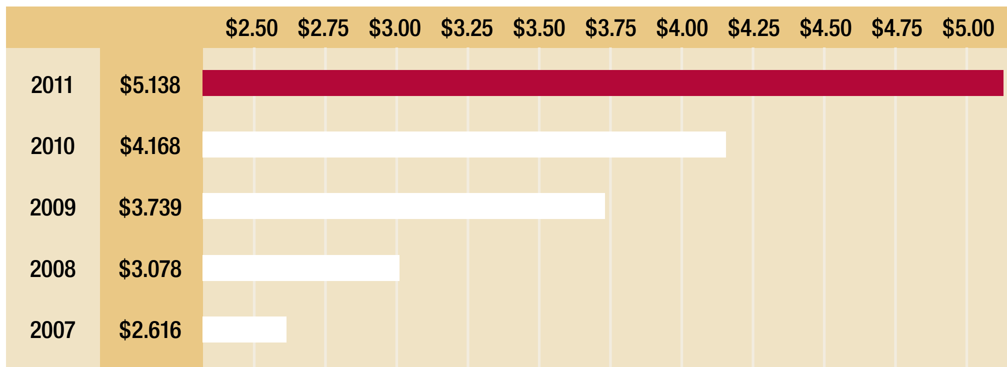
2011 Financial Highlights

Diana R. Johnson
Executive Vice President & Chief Financial Officer
Lyons Bancorp, Inc. and The Lyons National Bank

RESULTS OF OPERATIONS

For the year ended December 31, 2011, we recorded earnings of $5.1 million, an increase of $970,000 or 23.3% over 2010. This translates into earnings per diluted share of $3.76 for the year ended December 31, 2011, or a 16.0% increase year over year. Return on average assets was 0.96% versus 0.85% for 2010, and return on average equity was 14.47% versus 12.99% for 2010.

Net Income (year ending, in millions)



	2011			2010		
	Average Balance	**Interest Inc/Exp**	**Average Yield/Cost**	Average Balance	Interest Inc/Exp	Average Yield/Cost
Interest-earning assets:						
Loans:						
Residential real estate	**$ 127,526**	**$ 6,038**	**4.73%**	$ 106,358	$ 5,500	5.17%
Commercial and agriculture real estate	**98,813**	**5,212**	**5.27%**	92,521	5,232	5.65%
Commercial and agriculture loans	**75,171**	**3,716**	**4.94%**	70,500	3,599	5.10%
Consumer installment loans	**28,708**	**2,002**	**6.97%**	27,222	1,988	7.30%
Total loans	**330,218**	**16,968**	**5.14%**	296,601	16,319	5.50%
Investments	**162,408**	**4,870**	**3.00%**	151,931	5,066	3.33%
Federal funds sold and other interest- earning assets	**8,472**	**19**	**0.22%**	7,794	19	0.24%
Total interest-earning assets	**501,098**	**21,857**	**4.36%**	456,326	21,404	4.69%
Noninterest-earning assets	**33,825**			32,151		
Total assets	**$ 534,923**			$ 488,477		
Interest-bearing liabilities:						
Interest-bearing checking	**$ 50,092**	**$ 96**	**0.19%**	$ 43,319	$ 99	0.23%
Money market and savings accounts	**208,846**	**1,584**	**0.76%**	169,666	1,272	0.75%
Time deposits	**120,117**	**1,274**	**1.06%**	127,949	1,747	1.37%
Borrowings	**21,188**	**175**	**0.83%**	27,529	271	0.98%
Junior subordinated debentures	**9,217**	**524**	**5.69%**	8,786	341	3.88%
Total interest-bearing liabilities	**409,460**	**3,653**	**0.89%**	377,249	3,730	0.99%
Noninterest-bearing deposits	**86,267**			75,753		
Other noninterest-bearing liabilities	**3,637**			3,381		
Total liabilities	**499,364**			456,383		
Total equity	**35,559**			32,094		
Total liabilities and equity	**$ 534,923**			$ 488,477		
Net interest spread			**3.47%**			3.70%
Net interest income/margin on earning assets		**18,204**	**3.63%**		17,674	3.87%
Tax equivalent adjustment		**(642)**			(585)	
Net interest income per financial statements		**$ 17,562**			$ 17,089	

Our largest revenue source is net interest income, the difference between the interest income we earn on our interest-earning assets, primarily loans and investment securities, and the interest paid on our interest-bearing liabilities, primarily deposit accounts and borrowings. Net interest income for 2011 was $17.6 million, an increase of $473,000 or 2.8% over 2010. This increase was due primarily to strong growth of our earning assets funded by steady deposit growth, as average earning assets increased $44.8 million or 9.8% during 2011, and average interest-bearing deposits increased $38.1 million or 11.2% year over year. However, our tax-equivalent net interest margin decreased 24 basis points year over year, measuring 3.63% during 2011, compared to 3.87% in 2010. This decrease was due to lower reinvestment rates for loan and investment cash flows, while funding costs currently at low levels repriced more modestly.

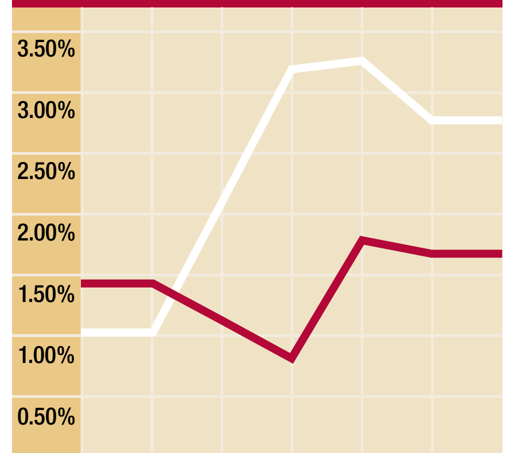
Our provisions for loan losses are based upon our assessment of a variety of factors, including loan credit quality, the general economic environment and growth in our loan portfolio. In 2011, we provided $965,000 for loan losses, compared to $2.4 million in 2010. The decrease in the provision for 2011 reflects the decrease in net charge-offs, and is reflective of improvement in asset quality ratios. At December 31, 2011 our nonperforming loans totaled 1.65% of total loans, as compared to 1.79% at December 31, 2010, and compares favorably to our peer's ratio of 2.78% at December 31, 2011. Our net charge offs to average loans during 2011 totaled 0.12%, compared to 0.30% during 2010 and 0.79% for our peers during 2011.

Noninterest income is an important revenue source for us, and consists primarily of service charges on deposit accounts, loan servicing fees, cardholder fees, financial services fees, gains and losses on the sale of securities, and gains on sale of loans. In 2011, noninterest income totaled $6.4 million or 26.6% of all revenue sources. This is an increase of $545,000 or 9.4% over 2010 levels. Most major categories of noninterest income saw improvement, with the exception of gains on sale of securities. During 2011, we sold $13.6 million of investment securities available for sale for a net gain of $407,000, while in 2010 we sold $35.6 million of securities available for sale for a net gain of $727,000.

Noninterest expense consists primarily of compensation and employee benefits, occupancy and equipment expenses, advertising, data processing, professional fees, FDIC insurance, and other operating expenses. In 2011, total noninterest expense was $16.1 million, an increase of $1.2 million or 8.2% over 2010. Increases in salaries and wages, pension and benefits, and occupancy expenses are primarily a reflection of a full year of expenses relating to the opening of our newest office in Seneca County. Most other operating expenses experienced modest increases in 2011 compared to 2010, with the exception of other expenses. The increase in other expenses is attributable to a number of initiatives currently taking place at LNB, including enhanced staff training, continued support of our local communities through contributions and sponsorships, as well as funding for our WOW! program.

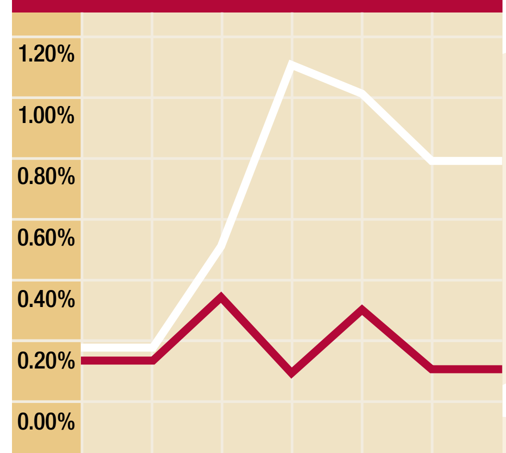
Nonperforming Loans to Total Loans

	2007	2008	2009	2010	2011
LNB	1.46%	1.09%	0.86%	1.79%	1.65%
Peer	1.04%	2.07%	3.18%	3.24%	2.78%



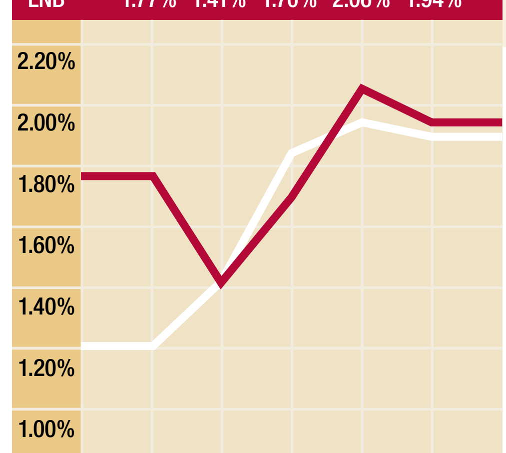
Net Charged-off Loans to Average Loans

	2007	2008	2009	2010	2011
LNB	0.14%	0.35%	0.11%	0.30%	0.12%
Peer	0.18%	0.53%	1.12%	1.01%	0.79%

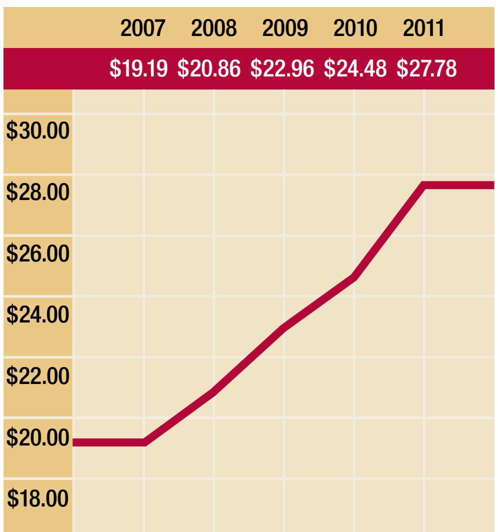


Allowance for Loan Losses/Total Loans

	2007	2008	2009	2010	2011
LNB	1.77%	1.41%	1.70%	2.06%	1.94%
Peer	1.21%	1.42%	1.85%	1.94%	1.89%



Book Value per Share



ANALYSIS OF FINANCIAL CONDITION

During 2011 we continued to experience solid loan and deposit growth. Total assets on December 31, 2011 were $555.5 million, an increase of $41.9 million or 8.2% over December 31, 2010.

Total loans were $360.0 million at December 31, 2011, an increase of $47.4 million or 15.1% from December 31, 2010. We continued to support our strategy of balancing the loan portfolio more evenly between consumer and commercial loans, ending the year with 48% consumer–related loans versus 52% commercial–related loans, ratios essentially unchanged from the prior year. We are well positioned to continue prudent lending to the individuals, families and businesses here in our Upstate New York marketplace and look forward to another year of solid loan growth.

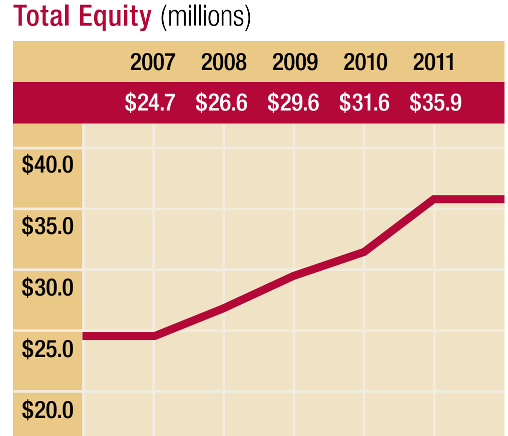
We maintain an investment portfolio to provide us with important liquidity considerations and earnings potential. Our investment portfolio consists primarily of United States Treasury bonds, United States Agency debt, mortgage-backed securities either guaranteed by the U.S. government or issued by the Federal Home Loan Bank, and state and local government debt. As of December 31, 2011, our investment portfolio totaled $154.6 million, a decrease of $7.9 million over December 31, 2010 and had an average tax-exempt yield of 3.00% during 2011. The decrease in our investment portfolio is due primarily to the utilization of investment cash flows to help support our loan growth. Substantially all of our investments are classified as available for sale, and may be used as collateral for public fund deposits.

Deposits generated within our local markets are the major source of funds for our lending and investment activities. Total deposits at December 31, 2011 were $461.0 million, an increase of $37.0 million or 8.7% over December 31, 2010. We continued to experience strong growth in our core deposit base, with our newest branch office in Seneca County contributing over $40 million in deposits since its opening in June 2010.

Total equity was $35.9 million at December 31, 2011, an increase of $4.3 million or 13.7% from December 31, 2010. Our Board of Directors is committed to providing a solid return to our shareholders and declared a total of $0.95 per share in dividends during 2011. This represents a yield of 3.56% based on our year end market price of $26.67 per share.

Please refer to our Consolidated Financial Report as of December 31, 2011 for more information regarding our 2011 results.

Total Equity (millions)



SELECTED FINANCIAL DATA	Year Ended December 31				
(In thousands, except per share data)	2011	2010	2009	2008	2007
Financial Statement Highlights					
Assets	$555,451	$513,585	$457,787	$411,490	$384,405
Loans, gross	359,951	312,629	288,226	245,457	217,834
Deposits	460,999	424,006	382,334	356,767	342,730
Other borrowings	42,058	44,491	36,046	17,642	7,489
Junior subordinated debentures	9,217	9,217	6,190	6,190	6,190
Total equity	35,894	31,567	29,571	26,600	24,681
Interest and dividend income	21,215	20,819	19,829	20,788	21,999
Interest expense	3,653	3,730	4,692	7,286	9,459
Net interest income	17,562	17,089	15,137	13,502	12,540
Provision for loan losses	965	2,405	1,725	405	250
Net securities gains	407	727	811	71	20
Net income	5,138	4,168	3,739	3,078	2,616
Per Share Information (1)					
Basic earnings per share	$3.98	$3.24	$2.93	$2.42	$2.04
Diluted earnings per share	$3.76	$3.24	$2.93	$2.42	$2.04
Cash dividends declared	$0.95	$0.89	$0.79	$0.76	$0.71
Book value per share	$27.78	$24.48	$22.96	$20.86	$19.19
Selected Ratios					
Return on average assets	0.96%	0.85%	0.86%	0.79%	0.71%
Return on average equity	14.47%	12.99%	13.13%	11.93%	11.42%
Leverage ratio (Bank)	8.42%	8.22%	8.01%	8.32%	8.24%
Dividend payout ratio	22.75%	26.97%	26.64%	30.77%	35.02%
Other Selected Data *(in whole numbers)*					
Employees (full time equivalent)	142	139	129	131	133
Banking Offices	11	11	10	10	10

(1) Per share data reflects 3-for-2 stock split on February 29, 2012.

Main Street Banking

LNB employee and Newark Fire Chief, Mike Colacino (far right) and wife, Marie, ride along with NYS Senator Michael Nozzolio (center) on the Newark Fire Department Float in the **Annual Newark Rose Parade**, one of the celebratory events of Newarkfest.

LNB Cools Off Local Library– LNB provided a generous contribution to the **Waterloo Library & Historical Society** to be used to install the final stages of the AC unit into the library. Shown in the photo from left to right are *President of the Waterloo Library and Historical Society,* Peter Houghton; LNB *Seneca County Branch Manager,* Jill Hansen; Bill Sigrist, *Trustee Member,* and *Executive Director,* Nancy Newland.

It's Our Way of Life.

Every day, LNB employees set out to make a difference in the communities where we live and work—whether it's volunteering in support of a local organization, sitting on a board, offering sponsorship support, or simply going the extra mile to brighten someone's day. We strive not only to serve our Main Street communities, but also to 'WOW!' them.

Newark branch staff Kathy Wind, *Assistant Branch Manager* (left) and Christina Valcore, *CSR* (right) deliver balloons to **DeMay Living Center** residents including Lillian Capron (center), at their annual **Chocolate Social on Valentine's Day**. All proceeds are allocated to the Center's activities program.

Tom Kime, *LNB EVP & Chief Operating Officer,* receives a welcoming handshake from dear friend, LNB Advisory Board member and owner of Wadhams Inc., Steve Wadhams at the **2011 Geneva Chamber Citizen of the Year Dinner**. Kime was recognized as the 2011 Geneva Chamber Citizen of the Year, celebrating an individual who has unselfishly given to the community and created a more dignified, unique place in which we all work and live.

He Shoots, He Scores!
The Rochester Wheels take on their toughest competition yet–the Wayne ARC Rimriders including (center) CJ Britt, *LNB EVP & Senior Lending Officer.* Jarrod Crawford and Lisa Mashewske, of LNB's Newark branch office, also played ball to support fundraising efforts of the Wayne ARC.

Ranking 3rd among Rochester banks for SBA lending, LNB was recently recognized by receiving a bronze plaque for its accomplishments.–(Left to right) Scott MacKenzie, *Commercial / AG Loan Officer;* Steve D'Orazio, *Commercial Loan Officer;* Jim King, *Commercial Loan Officer;* CJ Britt, *Senior Commercial Lending Officer;* Darrin Brentnall, *Commercial Loan Officer;* Malcolm Richards, *SBA;* Gregory MacDonald, *Commercial / AG Loan Officer;* and Anna Bridger, *Commercial Loan Officer.*

Play Ball! LNB employees Tara Rago, *Branch Manager* and Ashley Sindoni, *Marketing Assistant* throw the first pitch at the annual **LNB Geneva Red Wings Game Day**. LNB is a major sponsor of the Geneva Red Wings athletics program and is proud to support the new Geneva Twins baseball team.

It's Our Philosophy.

Our success is rooted in an unwavering commitment to Main Street banking practices. We pride ourselves on fiscal integrity, and stand committed to providing the unmatched level of service our customers deserve. As always, decisions are made locally and on an individual basis—as they should be.

Darlene Whitcomb, *LNB Branch Manager* presents LNB Customer, Dan LaGasse with a gift basket at the Branch Office's **25th Anniversary Celebration**. LaGasse was the first customer of the Branch Office on Rts. 14 & 31 in Lyons when it opened 25 years ago.

And It's Our Promise.

LNB has proudly served as your Main Street bank for 160 years! As we look forward to a future of steady growth, we remain dedicated to preserving our hometown values, and commitment to the people and communities that have supported our success.

LNB is a proud sponsor of the **Geneva Business Improvement District's Cruisin' Nights.** Pictured here with LNB customer Randy Delisio's Crazy Crate car are (left to right): Michelle VerStraete, *Head Teller;* Kate Decker, *Banking officer and Assistant Branch Manager;* Heidi Brown, *CSR;* Tara Rago, *AVP & Branch Manager;* and Jennifer Everett, *Head Teller.*

BOARD OF DIRECTORS

Robert A. Schick
President & Chief Executive Officer
Lyons Bancorp, Inc. & The Lyons National Bank

David J. Breen, Jr.
General Manager
Herrema's Market Place

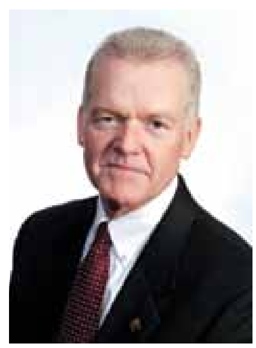
Clair J. Britt, Jr.
Executive Vice President & Senior Commercial Lending Officer
The Lyons National Bank

Joseph A. Fragnoli
Owner
Super Casuals

Andrew F. Fredericksen, CPA
Senior Partner
Fredericksen & Sirianni, LLP

Dale H. Hemminger
President & General Manager
Hemdale Farms & Greenhouses

James A. Homburger
Real Estate Broker



Thomas L. Kime
Executive Vice President & Chief Operating Officer
The Lyons National Bank

Brad A. Person
President & General Manager
Nuttall Golf Cars Inc. and Nuttall Golf Car Leasing, LLC

James E. Santelli
Retired Vice President & Co-owner
Santelli Lumber Co.

John J. Werner, Jr.
Retired President & Chief Executive Officer
Lyons Bancorp, Inc. & The Lyons National Bank

GENEVA ADVISORY BOARD

Stephen J. Blowers
Blowers Agri Service, Inc.

Peter J D'Amico, Jr.
D'Amico Chrysler Dodge Jeep

Jason S. Feinberg
Finger Lakes Health

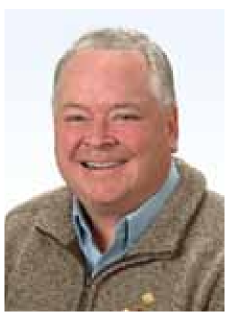
Robert S. Flowers
Hobart and William Smith Colleges

Carl W. Fribolin
White Springs Winery

Bernard G. Lynch
Lynch Furniture

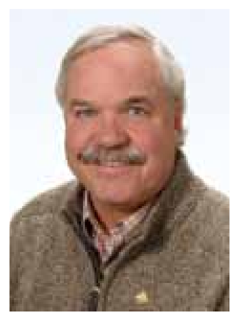
PENN YAN ADVISORY BOARD

Bonnie B. Curbeau
Curbeau Realty



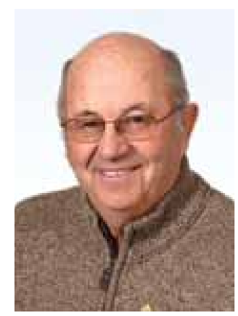
Michael D. Linehan
Yates County Chamber of Commerce

James H. Long
Longs' Cards and Books



Paul W. Marble, Jr.
Marble's Automotive and Glass

Steven D. Perry
Knapp & Schlappi Lumber Co., Inc.



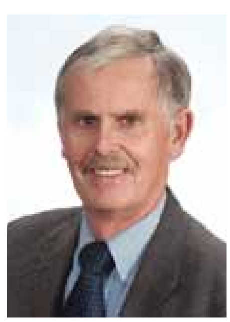
Neil J. Simmons
Simmons Vineyards

Not Pictured: **Henry Martin** *Town of Benton Dairy Farmer*

SENECA COUNTY ADVISORY BOARD

Salvatore N. Franzone
Ciccino's Pizzeria and Restaurant

Kenneth (Lee) Patchen, Jr.
Patchen Real Estate



Eugene Pierce
Glenora Wine Cellars, Inc. and Knapp Winery

Robert L. Sessler
Retired Business Owner

Jane M. Shaffer
Sessler Companies

Joyce N. Sinicropi
Sinicropi Florist

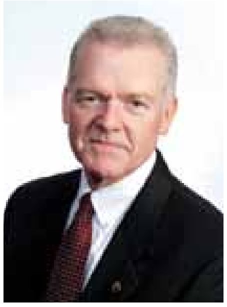
Stephen J. Wadhams
Wadhams Enterprises, Inc.

Bank Officers and Supervisors

EXECUTIVE MANAGEMENT

Robert A. Schick
President & Chief Executive Officer

Diana R. Johnson
Executive Vice President & Chief Financial Officer



Thomas L. Kime
Executive Vice President & Chief Operating Officer

Stephen V. DeRaddo
Executive Vice President & Senior Retail Lending Officer

Phillip M. McCann
Executive Vice President & Chief Credit Officer

Clair J. Britt, Jr.
Executive Vice President & Senior Commercial Lending Officer

ADMINISTRATION

Robert A. Schick
President & Chief Executive Officer

Thomas L. Kime
Executive Vice President & Chief Operating Officer

Carol A. Snook
Banking Officer & Corporate/Executive Secretary

AUDIT & COMPLIANCE

Ruth M. Columbus
Vice President & Director of Internal Audit

Joyce A. Marble
Assistant Vice President & Compliance/BSA Officer

Melonie L. Tiffany
Banking Officer & Staff Auditor

BRANCH DIVISION

Thomas D. Muller
Senior Vice President & Director of Retail Sales

Susan K. Andersen
Vice President & Branch Manager – Penn Yan

Jeffrey A. Friend
Vice President & District Branch Manager – Geneva and Seneca County

Jarrod D. Crawford
Assistant Vice President & Branch Manager – Newark

William L. Dungey
Assistant Vice President & Branch Manager – Clyde and Jordan

Jill D. Hansen
Assistant Vice President & Branch Manager – Seneca County

Tara R. Rago
Assistant Vice President & Branch Manager – Geneva

Sherri A. Sheldon
Assistant Vice President & Branch Manager – Wolcott

Jean E. Tsepas
Assistant Vice President & Branch Manager – Ontario

Darlene M. Whitcomb
Assistant Vice President & Branch Manager – Lyons

James S. Bilotta
Banking Officer & Branch Manager – Macedon

Kate E. Decker
Banking Officer & Assistant Branch Manager – Geneva

Cathy J. DeMay
Banking Officer & Assistant Branch Manager – Ontario

Shannon K. DeRosa
Banking Officer & Business Development Cash Manager Rep.

Julie B. Downey
Banking Officer & Assistant Branch Manager – Main Office

Susan L. Snyder
Banking Officer & Assistant Branch Manager – Penn Yan

Kathleen A. Wind
Banking Officer & Assistant Branch Manager – Newark

COMMERCIAL LENDING DIVISION

Clair J. Britt, Jr.
Executive Vice President & Senior Commercial Lending Officer

Stephen V. D'Orazio
Vice President & Commercial Loan Officer

James H. King
Vice President & Commercial Loan Officer

Scott A. MacKenzie
Vice President & Agricultural /Commercial Loan Officer

Anna M. Bridger
Assistant Vice President & Commercial Loan Officer

Gregory R. MacDonald
Assistant Vice President & Agricultural/Commercial Loan Officer

CREDIT ADMINISTRATION & COMMERCIAL LOAN OPERATIONS

Phillip M. McCann
Executive Vice President & Chief Credit Officer

Pamela J. Lee
Vice President & Portfolio Monitoring Officer

Jason Cornwell
Banking Officer & Senior Credit Underwriter

Lynnette M. Zelias
Banking Officer & Commercial Loan Operations Manager

FINANCE DIVISION

Diana R. Johnson
Executive Vice President & Chief Financial Officer

Brenda L. Cordero
Banking Officer & Accounting Manager

Chad J. Proper
Banking Officer & Financial Analyst

FINANCIAL SERVICES

Robert T. Koczent
Vice President & Director of Financial Services

HUMAN RESOURCES

Kimberly A. Kelley
Assistant Vice President & Director of Human Resources

Trevor Thomas
Assistant Vice President & Director of Training

MARKETING DIVISION

Shelly M. Nicoletta
Assistant Vice President & Director of Marketing

OPERATIONS & IT DIVISION

Todd F. Juffs
Assistant Vice President & MIS Officer

Cheryl M. Graham
Assistant Vice President & Policies and Procedures Manager

RETAIL LENDING DIVISION

Stephen V. DeRaddo
Executive Vice President & Senior Retail Lending Officer

Robert T. MacDonell
Vice President & Consumer Loan Officer

Joshua N. Miller
Vice President & Mortgage Loan Officer

Hope A. Alexanian
Assistant Vice President & Retail Loan Operations Manager

Thomas R. David
Assistant Vice President & Mortgage Loan Officer

Timothy H. Lead
Assistant Vice President & Mortgage Loan Officer

Angela M. Merola
Banking Officer & Collector

SECURITY & FACILITIES DIVISION

Michael J. Colacino
Security & Banking Officer and Facilities Manager

Family of the late Earl "Red" T. Wadhams (left to right): Rick Wadhams (son), Alice Wadhams (wife), Kathy Young (daughter), and Steve Wadhams (son).

In 2010 we expanded into Seneca County to better serve our local customer base. LNB entered the market on June 14, 2010 with an interim office on Routes 5 & 20 in Seneca Falls. Our permanent office, located at 2433 State Route 414 in Waterloo, opened January 7, 2011.

The new full-service branch offers a range of deposit and loan products, a drive-thru, 24-hour ATM, commercial lending, residential mortgage, and financial service offerings.

Introducing the LNB Seneca County Staff
(Left to right): Wendy Wright, *Assistant Branch Manager;* Michelle Verstraete, *CSR;* Danielle Smith, *CSR;* Paige Storrs, *Head Teller;* Jill Hansen, *AVP / Branch Manager;* Brenda Jewell, *Senior Teller;* Ginny Hill, *Teller;* and Krista Parmelee, *Mortgage Processor.* Not pictured, Jeff Friend, *VP / District Branch Manager.*

The 4,525 square-foot building also houses a community room, established in honor of the late Earl "Red" Wadhams for his distinction and involvement with the Seneca County community. The room features a tribute display that houses some of Red's favorite memorabilia including his John Deere collection, photos of tractor pulls he participated in with his family, as well as photos of spending time with those he loved most.

Prior to opening the new offices, LNB announced the appointment of the following individuals to serve as LNB Seneca County Advisory Board members: Daniele Bonafiglia-Wirth, *Vice President and Director of Finance for BonaDent Dental Laboratories;* Salvatore N. Franzone, *Chief Operating Officer and General Manager of Ciccino's;* Kenneth "Lee" Patchen, *Jr., Broker and Owner of Patchen Real Estate;* Gene Pierce, *President and CEO of Glenora Wine Cellars, Inc. and President of Knapp Vineyards;* Jane M. Shaffer, *Co-Owner of Sessler Companies;* Bryan vonHahmann, *President of Agri-Max Financial,* and the late Earl "Red" Wadhams, *Owner of Wadhams Inc.*

We have recently welcomed the following individuals to serve on this board: Robert L. Sessler, *Retired Business Owner;* Joyce N. Sinicropi, *Owner, Sinicropi Florist;* and Stephen J. Wadhams, *Owner, Wadhams Inc.*

The input and informed guidance of our Seneca County Advisory board have been tremendous assets to LNB in our quest to meet the needs of the individuals and businesses throughout the Seneca County area.

As President and CEO Bob Schick referred to in his President's Message, we have far outdone ourselves when it comes to better servicing our customer base in this market. Not only have we succeeded in this, but our new Seneca County branch exceeded our original 3-year growth plan in its first year of operation. We accomplished this by expanding services to our current customers, as well as developing many new-to-the-bank customers and relationships. Our staff has also been recognized for its superior service within the community and continues to be a leader in support for community programs and volunteerism. We look forward to continued growth and success in the Seneca County region.

Lyons Bancorp, Inc.

It's all about people.

Clyde Office
4 Williams Street
Clyde, NY 14433
(315) 923-2100

Geneva Office
399 Exchange Street
Geneva, NY 14456
(315) 781-5000

Jordan Office
2 North Main Street
Jordan, NY 13080
(315) 689-9530

Lyons Office
Corner Routes 14 & 31
Lyons, NY 14489
(315) 946-4505

Macedon Office
359 NYS Route 31
Macedon, NY 14502
(315) 986-9681

Main Office
35 William Street
Lyons, NY 14489
(315) 946-4871

Newark Office
750 West Miller Street
Newark, NY 14513
(315) 331-0296

Ontario Office
Tops Plaza
6256 Furnace Road
Ontario, NY 14519
(315) 524-9661

Penn Yan Office
205 Liberty Street
Penn Yan, NY 14527
(315) 536-2300

Seneca County Office
2433 State Route 414
Waterloo, NY 13165
(315) 539-4100

Wolcott Office
5996 New Hartford Street
Wolcott, NY 14590
(315) 594-6002

Front Cover Captions (from left to right):

As a rite of spring, Lyons CSD students drive tractors to school. As is the case in most rural areas, the School District is centric to everyday living. The Bank and District have built a strong partnership over the years.

Bank staff spent the day at the Wayne County Humane Society painting, gardening, and caring for the animals on the United Way's Annual Day of Caring. The Bank previously made the lead contribution for the purchase of "cat condos" at the Society.

Marty Burns, *President, Geneva Family YMCA Board of Directors*, is congratulated by LNB's Bob Schick, *President and CEO*, and Tara Rago, *Geneva Branch Manager*, at the ground breaking ceremony for the YMCA's new cardio area expansion towards which LNB provided a substantial contribution.

Jim King, *VP & Commercial Lender of LNB*, congratulates and thanks Mary Boatfield, *Happiness House Executive Director* and Eileen Gage, *Happiness House Board President* for working together to secure a $700,000 grant from the Federal Home Loan Bank of New York to provide housing and intermediate care for eight people at Happiness House's transition home.

LNB's expansion into the Seneca County market, a cornerstone project to further economic development within the region, commenced with a groundbreaking ceremony on September 14, 2010. The Seneca County Advisory Board including (pictured left to right) Sal Franzone, *Ciccino's Restaurant*; Jane Shaffer, *Sessler Companies*; Gene Pierce, *Knapp Winery and Glenora Wine Cellars*; Lee Patchen, *Patchen Real Estate*; Jill Hansen, *LNB AVP / Branch Manager*; and Jeff Friend, *LNB VP & District Branch Manager*, marked the event by helping to "break ground" on what would become the new 4,525 square foot full-service branch. *See inside "Special Feature" for full story.*

Mike Linehan, *LNB Penn Yan Advisory Board Member* and *President & CEO of the Yates County Chamber of Commerce*, has been a great asset to LNB through the years. Linehan, pictured here at an employee rally, currently serves on LNB's WOW! Factor Committee. The committee's focus is to improve and enhance the Bank's customer service profile.

BankwithLNB.com

Lyons Bancorp, Inc.
It's all about people.

Lyons Bancorp, Inc.

It's all about people.

Consolidated Financial Report

December 31, 2011

TABLE OF CONTENTS

ANNUAL MEETING

The annual meeting of the stockholders will take place at 4:30 p.m. on May 23, 2012 at the historic Ohmann Theatre in Lyons, New York.

Independent Auditors report goes here

CONSOLIDATED BALANCE SHEETS
December 31, 2011 and 2010

(In thousands)

ASSETS

		2011		2010
Cash and due from banks	$	13,749	$	8,679
Interest-bearing deposits in banks		5,326		7,000
Cash and Cash Equivalents		19,075		15,679
Investment securities:				
Available for sale		143,080		154,296
Held to maturity		7,558		5,306
Restricted equity securities, at cost		4,001		2,949
Total Investment Securities		154,639		162,551
Loans		359,951		312,629
Less allowance for loan losses		(7,001)		(6,441)
Net Loans		352,950		306,188
Land, premises and equipment, net		14,696		13,356
Bank owned life insurance		7,593		7,358
Accrued interest receivable and other assets		6,498		8,453
Total Assets	$	555,451	$	513,585

LIABILITIES AND EQUITY

		2011		2010
Liabilities				
Deposits:				
Interest-bearing	$	367,202	$	339,649
Noninterest-bearing		93,797		84,357
Total Deposits		460,999		424,006
Securities sold under agreements to repurchase		7,058		7,691
Borrowings from Federal Home Loan Bank		35,000		36,800
Junior subordinated debentures		9,217		9,217
Accrued interest payable and other liabilities		7,283		4,304
Total Liabilities		519,557		482,018
Equity				
Lyons Bancorp, Inc. stockholders' equity:				
Common stock		434		434
Paid-in capital		8,037		7,932
Retained earnings		28,477		24,569
Accumulated other comprehensive loss		(782)		(1,121)
Treasury stock, at cost		(328)		(303)
Total Lyons Bancorp, Inc. Stockholders' Equity		35,838		31,511
Noncontrolling interest		56		56
Total Equity		35,894		31,567
Total Liabilities and Equity	$	555,451	$	513,585

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF INCOME

Years Ended December 31, 2011 and 2010

(in thousands, except per share data)		**2011**		2010
Interest Income				
Loans	**$**	**16,968**	$	16,319
Investment securities:				
Taxable		**2,923**		3,288
Non-taxable		**1,324**		1,212
Total Interest Income		**21,215**		20,819
Interest Expense				
Deposits		**2,954**		3,118
Borrowings		**699**		612
Total Interest Expense		**3,653**		3,730
Net Interest Income		**17,562**		17,089
Provision for Loan Losses		**965**		2,405
Net Interest Income after Provision for Loan Losses		**16,597**		14,684
Noninterest Income				
Service charges on deposit accounts		**2,344**		2,150
Loan servicing fees		**954**		856
Cardholder fees		**780**		673
Financial services fees		**669**		513
Net realized gains from sales/calls of available for sale securities		**407**		727
Realized gains on loans sold		**743**		534
Earnings on investment in bank owned life insurance		**235**		228
Other		**241**		147
Total Noninterest Income		**6,373**		5,828
Noninterest Expense				
Salaries and wages		**6,799**		6,248
Pensions and benefits		**2,238**		2,023
Occupancy		**1,727**		1,643
Data processing		**1,038**		1,005
Professional fees		**888**		856
FDIC and OCC assessments		**645**		735
Advertising		**431**		409
Loan fees		**426**		367
Office supplies		**314**		271
Other		**1,562**		1,299
Total Noninterest Expense		**16,068**		14,856
Income before Income Taxes		**6,902**		5,656
Income Tax Expense		**1,760**		1,484
Net income attributable to noncontrolling interest and Lyons Bancorp, Inc.		**5,142**		4,172
Less: Net income attributable to noncontrolling interest		**4**		4
Net Income	**$**	**5,138**	$	4,168
Earnings Per Share – basic (1)	**$**	**3.98**	$	3.24
Earnings Per Share – diluted(1)	**$**	**3.76**	$	3.24

See notes to consolidated financial statements. (1) Per share amounts have been adjusted to reflect a 3-for-2 stock split, effective February 29, 2012.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
Years Ended December 31, 2011 and 2010

(In thousands, except per share data)

	Common Stock	Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Treasury Stock	Noncontrolling Interest	Total
Balance - January 1, 2010	$ 434	$ 7,915	$ 21,552	$ (80)	$ (306)	$ 56	$ 29,571
Comprehensive income:							
Net income	–	–	4,168	–	–	–	4,168
Change in unrealized net gain on securities available for sale, net of tax	–	–	–	(532)	–	–	(532)
Change in unrealized loss on pension and postretirement benefits, net of tax	–	–	–	(200)	–	–	(200)
Change in unrealized gain on interest rate swap, net of tax	–	–	–	(309)	–	–	(309)
Total Comprehensive Income							**3,127**
Purchase of treasury stock	–	–	–	–	(143)	–	(143)
Issuance of treasury stock	–	3	–	–	33	–	36
Deferred compensation shares awarded, net	–	14	–	–	108	–	122
Deferred compensation shares vested	–	–	–	–	5	–	5
Cash dividends declared, $0.89 (1) per share	–	–	(1,151)	–	–	–	(1,151)
Balance – December 31, 2010	**$ 434**	**$ 7,932**	**$ 24,569**	**$ (1,121)**	**$ (303)**	**$ 56**	**$ 31,567**
Comprehensive income:							
Net income	–	–	5,138	–	–	–	5,138
Change in unrealized net gain on securities available for sale, net of tax	–	–	–	1,910	–	–	1,910
Change in unrealized loss on pension and postretirement benefits, net of tax	–	–	–	(1,242)	–	–	(1,242)
Change in unrealized loss on interest rate swap, net of tax	–	–	–	(329)	–	–	(329)
Total Comprehensive Income							**5,477**
Purchase of treasury stock	–	–	–	–	(330)	–	(330)
Issuance of treasury stock	–	52	–	–	212	–	264
Deferred compensation shares awarded, net	–	53	–	–	92	–	145
Deferred compensation shares vested	–	–	–	–	1	–	1
Cash dividends declared, $0.95 (1) per share	–	–	(1,230)	–	–	–	(1,230)
Balance – December 31, 2011	**$ 434**	**$ 8,037**	**$ 28,477**	**$ (782)**	**$ (328)**	**$ 56**	**$ 35,894**

See notes to consolidated financial statements. (1) Per share amounts have been adjusted to reflect a 3-for-2 stock split, effective February 29, 2012.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2011 and 2010

(In thousands)		**2011**		2010
Cash Flows from Operating Activities				
Net income	**$**	**5,138**	$	4,168
Adjustments to reconcile net income to net cash provided by operating activities:				
Provision for loan losses		**965**		2,405
Earnings on investment in bank owned life insurance		**(235)**		(228)
Net realized gain from sales/calls of available for sale securities		**(407)**		(727)
Realized gains on loans sold		**(743)**		(534)
Gain on sale of real estate owned		**(72)**		-
Deferred compensation expense		**148**		139
Net amortization on securities		**1,238**		995
Depreciation and amortization		**756**		702
Deferred income tax benefit		**-**		(243)
Contribution to defined benefit pension plan		**(750)**		(1,200)
Decrease in accrued interest receivable and other assets		**2,247**		898
Increase in accrued interest payable and other liabilities		**434**		427
Loans originated for sale		**(41,763)**		(38,595)
Proceeds from sales of loans		**38,799**		39,407
Net Cash Provided by Operating Activities		**5,755**		7,614
Cash Flows from Investing Activities				
Purchases of securities available for sale		**(38,449)**		(118,020)
Proceeds from sales of securities available for sale		**13,620**		35,644
Proceeds from maturities and calls of securities available for sale		**38,448**		55,514
Purchases of held to maturity securities		**(5,685)**		(2,563)
Proceeds from maturities of securities held to maturity		**3,383**		2,035
Net increase in restricted equity securities		**(1,052)**		(525)
Net increase in loans		**(44,024)**		(25,755)
Proceeds from sale of real estate owned		**169**		-
Purchase of bank owned life insurance		**-**		(500)
Premises and equipment purchases, net		**(2,094)**		(2,357)
Net Cash Used in Investing Activities		**(35,684)**		(56,527)
Cash Flows from Financing Activities				
Net increase in demand and savings deposits		**39,931**		53,309
Net decrease in time deposits		**(2,938)**		(11,637)
Net decrease in securities sold under agreements to repurchase		**(633)**		(1,255)
Net (decrease) increase in overnight borrowings from Federal Home Loan Bank		**(10,800)**		9,700
Proceeds received from issuance of trust preferred securities		**-**		2,932
Proceeds received from term borrowings from Federal Home Loan Bank		**15,000**		-
Repayment of term borrowings from Federal Home Loan Bank		**(6,000)**		-
Purchase of treasury stock		**(330)**		(143)
Issuance of treasury stock		**264**		36
Dividends paid		**(1,169)**		(1,124)
Net Cash Provided by Financing Activities		**33,325**		51,818
Net Increase in Cash and Cash Equivalents		**3,396**		2,905
Cash and Cash Equivalents – Beginning		**15,679**		12,774
Cash and Cash Equivalents – Ending	**$**	**19,075**	$	15,679
Supplementary Cash Flow Information				
Interest paid	**$**	**3,682**	$	3,742
Income taxes paid	**$**	**1,337**	$	2,423
Non-cash Disclosure				
Transfer of loans to foreclosed real estate	**$**	**4**	$	198

See notes to consolidated financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Lyons Bancorp, Inc. (the Company) provides a full range of commercial banking services to individual and small business customers through its wholly-owned subsidiary, The Lyons National Bank (the Bank). The Bank's operations are conducted in eleven branches located in Wayne, Onondaga, Yates, Ontario, and Seneca Counties, New York. The Company and the Bank are subject to the regulations of certain federal agencies and undergo periodic examinations by those regulatory authorities.

The Company owns all of the voting common shares of Lyons Capital Statutory Trust I (Trust I), Lyons Capital Statutory Trust II (Trust II) and Lyons Statutory Trust III (Trust III). Trust I was formed in 2003, Trust II was formed in 2004, and Trust III was formed in 2009. The Trusts were each formed for the purpose of securitizing trust preferred securities, the proceeds of which were advanced to the Company and contributed to the Bank as additional capital.

The Bank owns all of the voting stock of Lyons Realty Associates Corp. (LRAC) and, prior to December 2011, LNB Life Agency, Inc. (LNB Life). LRAC is a real estate investment trust which holds a portfolio of real estate mortgages. In order to maintain its status as a real estate investment trust, LRAC holds the real estate mortgages until they are paid. The real estate mortgages held by LRAC are included in loans on the consolidated balance sheet. LNB Life provided non-insured financial services and products to the Bank's customers. LNB Life was dissolved in December 2011 as the Bank discontinued offering these products and services to customers.

Basis of Consolidation

The consolidated financial statements include the accounts of the Company, the Bank, LRAC and LNB Life. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accounts of Trust I, Trust II, and Trust III are not included in the consolidated financial statements as discussed in Note 9.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near future relate to the determination of the allowance and provision for loan losses, other-than-temporary impairment of investment securities, actuarial assumptions associated with the Company's benefit plans and deferred tax assets and liabilities.

Recently Issued Accounting Pronouncements

In April 2011, the FASB issued ASU 2011-02, *Receivables (Topic 310), A Creditor's Determination of Whether a Restructuring Is a Troubled Debt Restructuring*. This Update provides additional guidance and clarification to help creditors in determining whether a creditor has granted a concession and whether a restructuring constitutes a troubled debt restructuring (TDR). This Update was effective for the first interim or annual period beginning on or after June 15, 2011, with retrospective application to the beginning of the annual period of adoption. The measurement of impairment should be done retrospectively in the period of adoption for loans that are newly identified as TDR's upon adoption of this Update. In addition, the TDR disclosures required by ASU 2010-20, Receivables (Topic 310), *Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses*, are required beginning in the period of adoption of this Update. The adoption of this Update did not have a material impact on its consolidated financial statements.

Recently Issued Accounting Pronouncements (Continued)

In April 2011, the FASB issued ASU No. 2011-03, *Transfers and Servicing (Topic 860) Reconsideration of Effective Control for Repurchase Agreements*. This Update revises the criteria for assessing effective control for repurchase agreements and other agreements that both entitle and obligate a transferor to repurchase or redeem financial assets before their maturity. The determination of whether the transfer of a financial asset subject to a repurchase agreement is a sale is based, in part, on whether the entity maintains effective control over the financial asset. This Update removes from the assessment of effective control: the criterion requiring the transferor to have the ability to repurchase or redeem the financial asset on substantially the agreed terms, even in the event of default by the transferee, and the related requirement to demonstrate that the transferor possesses adequate collateral to fund substantially all the cost of purchasing replacement financial assets. The amendments in this Update are effective for interim and annual reporting periods beginning on or after December 15, 2011. The amendments are applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date and early adoption is permitted. The adoption of this guidance is not expected to have a material impact on the Company's consolidated financial condition or result of operations.

In May 2011, the FASB issued ASU 2011-04, *Fair Value Measurement (Topic 820), Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS*. The guidance clarifies and expands the disclosures pertaining to unobservable inputs used in Level 3 fair value measurements, including the disclosure of quantitative information related to (1) the valuation processes used, (2) the sensitivity of the fair value measurement to changes in unobservable inputs and the interrelationships between those unobservable inputs, and (3) use of a nonfinancial asset in a way that differs from the asset's highest and best use. The amendments are effective for annual periods beginning after December 15, 2011. The Company does not expect this pronouncement to have a material effect on its consolidated financial statements.

Earlier this year, the FASB issued ASU No. 2011-05, *Comprehensive Income (Topic 220): Presentation of Comprehensive Income* (ASU 2011-05). ASU 2011-05 was intended to increase the prominence of other comprehensive income in financial statements and help financial statement users better understand the cause of a company's change in financial position and results of operations. Stakeholders, however, recently raised concerns that new presentation requirements about the reclassification of items out of accumulated other comprehensive income would be costly for preparers and add unnecessary complexity to financial statements. ASU 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05* (ASU 2011-12), defers the specific requirement to present items that are reclassified from accumulated other comprehensive income to net income separately with their respective components of net income and other comprehensive income. ASU 2011-12 did not defer the requirement to report comprehensive income either in a single continuous statement or in two separate but consecutive financial statements.

ASU 2011-05 and ASU 2011-12 are effective for public entities for fiscal years, and interim periods within those years, beginning after December 15, 2011. Management does not expect the adoption of this statement to have a material impact on the Company's consolidated financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investment Securities

Securities are classified as held to maturity and carried at amortized cost when management has the positive intent and ability to hold them until maturity. Securities to be held for indefinite periods of time are classified as available for sale and carried at fair value, with the unrealized holding gains and losses reported as a component of other comprehensive income, net of tax. Securities held for resale for liquidity purposes are classified as trading and are carried at fair value, with changes in unrealized holding gains and losses included in income. Management determines the appropriate classification of securities at the time of purchase. Restricted equity securities consist primarily of Federal Reserve Bank and the Federal Home Loan Bank stock.

Purchase premiums and discounts are recognized in interest income using the interest method or methods that approximate the interest method over the terms of the securities. Interest and dividends on securities are recognized in interest income using the interest method over the terms of the securities. Gains and losses on the sale of securities are determined using the specific identification method.

On a quarterly basis, the Company performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment. A security is considered impaired if the fair value is less than its amortized cost basis at the reporting date. If impaired, the Company then assesses whether the unrealized loss is other-than-temporary. The assessment considers (i) whether the Company intends to sell the security prior to recovery and/or maturity, (ii) whether it is more likely than not that the Company will have to sell the security prior to recovery and/or maturity and (iii) if the present value of the expected cash flows is not sufficient to recover the entire amortized cost basis. If a debt security is deemed to be other-than-temporarily impaired, the credit loss component of an other-than-temporary impairment write-down is recorded in earnings while the remaining portion of the impairment loss is recognized, net of tax, in other comprehensive income provided that the Company does not intend to sell the underlying security and it is more-likely-than not that the Company would not have to sell the security prior to recovery.

The Company considers the following factors in determining whether a credit loss exists and the period over which the security is expected to recover:

- The length of time and the extent to which the fair value has been less than the amortized cost basis;
- The level of credit enhancement provided by the structure which includes, but is not limited to, credit subordination positions, excess spreads, overcollateralization, protective triggers;
- Changes in the near term prospects of the issuer or underlying collateral of a security, such as changes in default rates, loss severities given default and significant changes in prepayment assumptions;
- The level of excess cash flow generated from the underlying collateral supporting the principal and interest payments of the debt securities; and
- Any adverse change to the credit conditions of the issuer of the security such as credit downgrades by the rating agencies.

Loans

The Bank grants real estate, commercial and consumer loans to its customers. A substantial portion of the loan portfolio is represented by real estate loans in Wayne, Ontario, Yates, Onondaga, and Seneca Counties. The Company's loan portfolio includes residential real estate, commercial real estate, agricultural real estate, commercial and agricultural loans, and consumer installment classes. Residential real estate loans include classes for 1-4 family and home equity loans. Consumer installment loans include classes for direct and indirect loans.

Loans (Continued)

Loans that management has the intent and ability to hold for the foreseeable future or until maturity or payoff are stated at their outstanding unpaid principal balances, net of an allowance for loan losses and any deferred fees or costs. Interest income is accrued on the unpaid principal balance. Loan origination fees, net of certain direct origination costs, are deferred and recognized as an adjustment of the yield (interest income) of the related loans. The Bank is generally amortizing these amounts over the contractual life of the loan. Premiums and discounts on purchased loans are amortized as adjustments to interest income using the effective yield method.

Interest income is accrued on the unpaid principal balance. The accrual of interest on loans is discontinued at the time the loan is 90 days past due unless the credit is well-secured and in process of collection. Credit card loans and other personal loans are typically charged off no later than 180 days past due. Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual or charged-off at an earlier date if collection of principal or interest is considered doubtful. All interest accrued but not collected for loans that are placed on nonaccrual or charged off is reversed against interest income or the allowance for loan losses if the interest income was earned in a prior period. The interest on these loans is accounted for on the cash-basis or cost-recovery method, until qualifying for return to accrual. Loans are returned to accrual status when all the principal and interest amounts contractually due are brought current and future payments are reasonably assured.

Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a loan to be impaired when it is probable that the Company will be unable to collect all amounts due according to the contractual terms of the loan agreement. When a loan is considered to be impaired, the amount of the impairment is measured based on the present value of expected future cash flows discounted at the loan's effective interest rate, or at the loan's observable fair value or the fair value of underlying collateral if the loan is collateral-dependent. Impairment losses are included in the allowance for loan losses through a charge to the provision for loan losses. Cash receipts on impaired loans are generally applied to reduce the principal balance outstanding. In considering loans for evaluation of impairment, management generally excludes smaller balance, homogeneous loans: residential mortgage loans, home equity loans, and all consumer loans, unless subject to a troubled debt restructuring. These loans are collectively evaluated for risk of loss.

Loans Held for Sale

Generally, loans held for sale consist of residential mortgage loans that are originated and are intended to be sold through agreements the Bank has with the Federal Home Loan Bank (FHLB) and the Federal Home Loan Mortgage Corporation (Freddie Mac). From time to time, the Bank may also hold commercial loans for sale. Realized gains and losses on sales are computed using the specific identification method. These loans are carried on the consolidated balance sheet at the lower of cost or estimated fair value determined in the aggregate. Loans held for sale totaled $4.6 million and $857,000 at December 31, 2011 and 2010, respectively, and are included in loans on the consolidated balance sheets.

During 2011 and 2010, the Company sold residential mortgage loans totaling $38.8 million and $39.4 million, respectively, and realized gains on these sales were $743,000 and $534,000, respectively. These residential real estate loans are generally sold without recourse in accordance with standard secondary market loan sale agreements. When residential mortgage loans are sold, the Company typically retains all servicing rights, which provides the Company with a source of fee income. In connection with the sales in 2011 and 2010, the Company recorded mortgage-servicing assets of $225,000 and $227,000, respectively. Amortization of mortgage servicing assets amounted to $185,000 in 2011 and $174,000 in 2010. Net mortgage-servicing assets included in the consolidated balance sheets totaled $462,000 and $422,000 net of amortization, as of December 31, 2011 and 2010, respectively. Total loans serviced for others amounted to $136.1 million and $121.3 million at December 31, 2011 and 2010, respectively.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Allowance for Loan Losses

The allowance for loan losses (allowance) is established as losses are estimated to have occurred in the loan portfolio. The allowance is recorded through a provision for loan losses charged to earnings. Loan losses are charged against the allowance when management believes the uncollectibility of a loan balance is confirmed. Subsequent recoveries, if any, are credited to the allowance.

The allowance is evaluated on a regular basis by management and is based upon management's periodic review of the collectibility of the loans in light of historical experience, the nature and volume of the loan portfolio, adverse situations that may affect the borrower's ability to repay, estimated value of any underlying collateral and prevailing economic conditions. This evaluation is inherently subjective as it requires estimates that are susceptible to significant revision as more information becomes available.

The allowance consists of general, specific and unallocated components as further described below.

General Component

The general component of the allowance is based on historical loss experience adjusted for qualitative factors stratified by the following loan classes: residential real estate, commercial real estate, agricultural real estate, commercial and agricultural loans, and consumer installment segments. Management uses a rolling average of historical losses based on a time frame appropriate to capture relevant loss data for each loan segment. The historical loss factor is adjusted for the following qualitative factors: levels and trends in delinquencies; trends in volume and terms of loans; effects of changes in risk selection and underwriting standards and other changes in lending policies, procedures and practices; experience/ability/depth of lending management and staff; and national and local economic trends and conditions. There were no changes in the Company's policies or its methodology pertaining to the general component of the allowance during 2011.

The qualitative factors are determined based on the various risk characteristics of each loan type. Risk characteristics relevant to each loan type are as follows:

Residential real estate - The Company generally does not originate loans with a loan-to-value ratio greater than 80 percent and does not grant subprime loans. The majority of loans in this segment are collateralized by owner-occupied residential real estate and repayment is dependent on the credit quality of the individual borrower. The overall health of the economy, including unemployment rates and housing prices, will have an effect on the credit quality in this class.

Commercial real estate - Loans in this class represent both extensions of credit for owner-occupied real estate and income-producing properties throughout the local region. The underlying cash flows of the operating commercial businesses (owner-occupied) and income properties (non-owner occupied) can be adversely impacted by a downturn in the economy as evidenced by increased vacancy rates, which in turn, will have an effect on the credit quality in this class. In a majority of cases, the Company obtains rent rolls annually and continually monitors the cash flows of non-owner occupied loans commensurate with sound lending practices.

Agricultural real estate - Loans in this class represent extensions of credit for owner-occupied agricultural real estate throughout the local region. The underlying cash flows generated by the agribusinesses can be adversely impacted by adverse climate and a weakened economy, which in turn, will have an effect on the credit quality in this class. Management obtains annual tax returns and continually monitors the cash flows of these loans commensurate with sound lending practices.

Allowance for Loan Losses (Continued)

Commercial and Agricultural loans – Loans in these classes are made to businesses and generally secured by the assets of the business. Repayment is expected from the cash flows of the business. A weakened economy, and resultant decreased consumer spending, will have an effect on the credit quality in this class.

Consumer installment loans – Loans in this segment may be secured or unsecured and repayment is dependent on the credit quality of the individual borrower. Unemployment rates will have an effect on the credit quality in this class.

Specific Component

The specific component relates to loans that are classified as impaired. Impairment is measured on a loan by loan basis for commercial and agricultural loans, commercial real estate and agricultural real estate by either the present value of expected future cash flows discounted at the loan's effective interest rate or the fair value of the collateral, less costs to sell, if determined to be more appropriate. An allowance is established when the discounted cash flow or collateral value of the impaired loan is lower than the carrying value of that loan. Large groups of smaller balance homogeneous loans are collectively evaluated for impairment. Accordingly, the Company does not separately identify individual consumer or residential real estate loans for impairment disclosures, unless such loans are subject to a troubled debt restructuring agreement.

A loan is considered impaired when, based on current information and events, it is probable that the Company will be unable to collect the scheduled payments of principal or interest when due according to the contractual terms of the loan agreement. Factors considered by management in determining impairment include payment status, collateral value, and the probability of collecting scheduled principal and interest payments when due.

All impaired loans require appraisals and/or chattel evaluations within 180 days of impairment, unless existing evaluation is less than 24 months old and no market or physical deterioration is noted. Re-appraisals and/or re-evaluations should be conducted whenever deemed appropriate, but typically recommended on a 24 month cycle if repayment is predicated upon liquidation of collateral and evidence suggests collateral values may have deteriorated.

Loans that experience insignificant payment delays and payment shortfalls generally are not classified as impaired. Management determines that significance of payment delays and payment shortfalls on a case-by-case basis, taking into consideration all of the circumstances surrounding the loan and the borrower, including the length of the delay, the reason for the delay, the borrower's prior payment record, and the amount of the shortfall in relation to the principal and interest owed.

Unallocated Component

An unallocated component is maintained to cover uncertainties that could affect management's estimate of probable losses. The unallocated component of the allowance reflects the margin of imprecision inherent in the underlying assumptions used in the methodologies for estimating allocated and general reserves in the portfolio.

Troubled Debt Restructurings

A modification of a loan constitutes a troubled debt restructuring ("TDR") when a borrower is experiencing financial difficulty and the modification constitutes a concession. Loans modified in a TDR often involve temporary interest-only payments, term extensions, reducing the interest rate

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Troubled Debt Restructurings (Continued)

for the remaining term of the loan, extending the maturity date at an interest rate lower than the current market rate for new debt with similar risk, requesting additional collateral, releasing collateral for consideration, or substituting or adding a new borrower or guarantor.

All of the loans identified as TDRs by the Company in 2011 and 2010 were previously on nonaccrual status and reported as impaired loans prior to restructuring. All loans restructured during 2011 are on nonaccrual status as of December 31, 2011. Nonaccrual loans that are restructured remain on nonaccrual status, but may move to accrual status after they have performed according to the restructured terms for a period of time of at least six months. The TDR classification did not have a material impact on the Company's determination of the allowance for loan losses because the modified loans were impaired and evaluated for a specific allowance both before and after restructuring.

Land, Premises and Equipment

Land is stated at cost. Premises and equipment are recorded at cost and are generally depreciated by the straight-line method over the estimated useful lives of the assets. Buildings are generally depreciated over a useful life of thirty nine and one half years, furniture and equipment over a useful life of three to seven years, and leasehold improvements over the lesser of the asset's useful life or the term of the lease.

Bank Owned Life Insurance

Bank owned life insurance (BOLI) was purchased by the Bank as a financing tool for employee benefits and to fund discriminatory retirement benefits for the Board of Directors and executive management. The value of life insurance financing is the tax preferred status of increases in life insurance cash values and death benefits and the cash flow generated at the death of the insured. The proceeds or increases in cash surrender value of the life insurance policy results in tax-exempt income to the Company. The largest risk to the BOLI program is credit risk of the insurance carriers. To mitigate this risk, annual financial condition reviews are completed on all carriers. BOLI is stated on the Company's consolidated balance sheets at its current cash surrender value. Increases in BOLI's cash surrender value are reported as noninterest income in the Company's consolidated statements of income.

Foreclosed Real Estate

Included in other assets are real estate properties acquired through, or in lieu of, loan foreclosure. These properties are initially recorded at fair value less estimated selling costs at the date of foreclosures. Any write-downs based on the asset's fair value at date of foreclosure are charged to the allowance for loan losses. After foreclosure, property held for sale is carried at the lower of the new basis or fair value less any costs to sell. Costs of significant property improvements are capitalized, whereas costs relating to holding property are expensed. Valuations are periodically performed by management, and any subsequent write-downs are recorded as a charge to operations, if necessary, to reduce the carrying value of the property to the lower of its cost or fair value less cost to sell. There was no foreclosed real estate at December 31, 2011. Foreclosed real estate at December 31, 2010 was $197,000.

Treasury Stock

Treasury stock is recorded at cost. Shares are reissued on the average cost method, except for issuance of deferred compensation shares, which are discussed in Note 12.

Interest Rate Swap Agreement

The Company utilizes an interest rate swap agreement as part of its management of interest rate risk to modify the repricing characteristics of its floating-rate junior subordinate debentures. For this swap agreement, amounts receivable or payable are recognized as accrued under the

Interest Rate Swap Agreement (Continued)

terms of the agreement, and the net differential is recorded as an adjustment to interest expense of the related debentures. The interest rate swap agreement is designated as a cash flow hedge. Therefore, the effective portion of the swap's unrealized gain or loss was initially recorded as a component of other comprehensive income, net of tax. The ineffective portion of the unrealized gain or loss, if any, is immediately reported in other operating income. The Company considers its interest rate swap agreement to be fully effective and accordingly it has not recorded any gains or losses in earnings during 2011 or 2010.

Advertising Costs

Advertising costs are expensed as incurred.

Noncontrolling Interest

Noncontrolling interest represents the portion of ownership and interest expense that is attributable to the minority owners of LRAC. The minority ownership is in the form of 8.50% cumulative preferred stock, and the dividends paid are included in noncontrolling interest as a charge against income.

Income Taxes

Income taxes are provided for the tax effects of certain transactions reported in the consolidated financial statements. Income taxes consist of taxes currently due plus deferred taxes related primarily to temporary differences between the financial reporting and income tax basis of the allowance for loan losses, premises and equipment, and prepaid and accrued employee benefits. The deferred tax assets and liabilities represent the future tax return consequences of the temporary differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred tax assets and liabilities are reflected at income tax rates applicable to the period in which the deferred tax assets and liabilities are expected to be realized or settled. As changes in tax laws or rates are enacted, deferred tax assets and liabilities are adjusted through the provision for income taxes. The Company recognizes interest and penalties accrued on any unrecognized tax benefits as a component of income tax expense.

Transfers of Financial Assets

Transfers of financial assets are accounted for as sales when control over the assets has been surrendered. Control over transferred assets is deemed to be surrendered when (1) the assets have been isolated from the Company, (2) the transferee obtains the right (free of conditions that constrain it from taking advantage of that right) to pledge or exchange the transferred assets, and (3) the Company does not maintain effective control over the transferred assets through an agreement to repurchase them before their maturity.

Earnings Income Per Share

Basic earnings per share represents income available to common shareholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflects additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as adjustments to net income for interest expense relating to convertible securities, net of tax, that would result from the assumed issuance. Treasury shares are not deemed outstanding for earnings per share calculations. See Note 13 for earnings per share calculations.

Statements of Cash Flows

For the purpose of presentation in the consolidated statements of cash flows, cash and cash equivalents are defined as the sum of cash and due from banks, federal funds sold, and interest-bearing deposits in banks with an original maturity of less than three months.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Off-Balance-Sheet Financial Instruments

In the ordinary course of business, the Bank has entered into off-balance-sheet financial instruments consisting of commitments to extend credit and standby letters of credit. Such financial instruments are recorded in the consolidated financial statements when they are funded or related fees are incurred or received.

Segment Reporting

The Company has evaluated the activities relating to its strategic business units, and determined that these strategic business units are similar in nature, and managed accordingly. The strategic business units are not reviewed separately to make operating decisions or assess performance. Therefore, the Company has determined it has no reportable segments.

NOTE 2 - RESTRICTIONS ON CASH AND DUE FROM BANKS

The Bank is required to maintain reserve funds in cash and/or on deposit with the Federal Reserve Bank. The required reserve at December 31, 2011 and 2010 was $8.0 million and $8.3 million, respectively.

The Bank is also required to maintain clearing balance funds on deposit with the Federal Reserve Bank. The required minimum clearing balance at December 31, 2011 and 2010 was $600,000.

NOTE 3 - INVESTMENTS

The amortized cost and fair value of investment securities, with gross unrealized gains and losses, are as follows at December 31, 2011 and 2010:

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2011:				
Available for Sale:				
United States treasuries	$ 5,066	$ 89	$ -	$ 5,155
United States agencies	29,639	1,173	-	30,812
State and local governments	49,933	1,476	-	51,409
Mortgage-backed securities	54,759	954	(9)	55,704
Total Available for Sale	$ 139,397	$ 3,692	$ (9)	$ 143,080
Held to Maturity:				
Local governments	$ 7,558	$ -	$ -	$ 7,558
Restricted Equity Securities	$ 4,001	$ -	$ -	$ 4,001

(In thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
December 31, 2010:				
Available for Sale:				
United States treasuries	$ 13,259	$ -	$ (282)	$ 12,977
United States agencies	27,440	27	(451)	27,016
State and local governments	52,547	986	(243)	53,290
Mortgage-backed securities	60,551	938	(476)	61,013
Total Available for Sale	$ 153,797	$ 1,951	$ (1,452)	$ 154,296
Held to Maturity:				
Local governments	$ 5,306	$ -	$ -	$ 5,306
Restricted Equity Securities	$ 2,949	$ -	$ -	$ 2,949

All of the above mortgage-backed securities are residential direct pass through securities or collateralized mortgage obligations issued or backed by government sponsored enterprises (GSEs). Restricted equity securities primarily include non-marketable Federal Home Loan Bank New York (FHLBNY) stock and non-marketable Federal Reserve Bank (FRB) stock, both of which are required to be held for regulatory purposes and for borrowing availability. The required investment in FHLBNY stock is tied to both the Company's borrowing levels with the FHLB and commitments to sell residential mortgage loans to the FHLB. Holdings of FHLBNY stock and FRB stock totaled $3.2 million and $380,000 at December 31, 2011, respectively, and $2.2 million and $380,000 at December 31, 2010, respectively. These securities are carried at par, which is also cost. Restricted equity securities also include miscellaneous investments carried at par, which is also cost.

Restricted equity securities are held as a long-term investment and value is determined based on the ultimate recoverability of the par value. Impairment of these investments is evaluated quarterly and is a matter of judgment that reflects management's view of the issuer's long-term performance, which includes factors such as the following: its operating performance; the severity and duration of declines in the fair value of its net assets related to its capital stock amount; its commitment to make payments required by law or regulation and the level of such payments in relation to its operating performance; and its liquidity and funding position. After evaluating these considerations, the Company concluded that the par value of these investments will be recovered and, as such, has not recognized any impairment on its holdings of restricted equity securities.

NOTE 3 - INVESTMENTS (Continued)

The following table sets forth the Company's investment in securities with unrealized losses of less than twelve months and unrealized losses of twelve months or more at December 31:

December 31, 2011:						
(In thousands)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
United States treasuries	$ -	$ -	$ -	$ -	$ -	$ -
United States agencies	-	-	-	-	-	-
State and local governments	-	-	-	-	-	-
Mortgage-backed securities	4,380	9	-	-	4,380	9
	$ 4,380	$ 9	$ -	$ -	$ 4,380	$ 9

December 31, 2010:						
(In thousands)	Less than 12 Months		12 Months or More		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
United States treasuries	$ 12,977	$ 282	$ -	$ -	$ 12,977	$ 282
United States agencies	16,920	451	-	-	16,920	451
State and local governments	11,203	242	569	1	11,772	243
Mortgage-backed securities	23,184	476	-	-	23,184	476
	$ 64,284	$ 1,451	$ 569	$ 1	$ 64,853	$ 1,452

On a quarterly basis, the Company performs an assessment to determine whether there have been any events or economic circumstances indicating that a security with an unrealized loss has suffered other-than-temporary impairment. Consideration is given to (1) the length of time and the extent to which the fair value has been less than the amortized cost basis, (2) the financial condition of the issuer (and guarantor, if any) and adverse conditions specifically related to the security, industry or geographic area, (3) failure of the issuer of the security to make scheduled interest or principal payments, (4) any changes to the rating of a security by a rating agency, (5) the presence of credit enhancements, if any, including the guarantee of the federal government or any of its agencies, (6) whether the Company intends to sell or more likely than not be required to sell the debt security, and (7) if the present value of the expected cash flow is not sufficient to recover the entire amortized cost.

There were two securities with unrealized losses for less than twelve months at December 31, 2011, while at December 31, 2010 there were fifty-five securities with losses for less than twelve months and one security with losses greater than twelve months. Substantially all of the unrealized losses on the Company's securities were caused by market interest rate changes from those in effect when the securities were purchased by the Company. The contractual terms of these securities do not permit the issuer to settle the securities at a price less than par value. Except for certain state and local government obligations, all securities rated by an independent rating agency carry an investment grade rating. Financial information relating to unrated state and government obligations is reviewed for indications of adverse conditions that may indicate other-than-temporary impairment. Because the Company does not intend to sell the securities with unrealized losses and it believes it is not likely to be required to sell the securities before recovery of their amortized cost basis, which may be, and is likely to be, maturity, the Company does not consider these securities to be other-than-temporarily impaired at December 31, 2011. In addition, there were no other-than-temporarily impaired charges in 2011 and 2010.

The amortized cost and fair value of debt securities at December 31, 2011, by contractual maturity, are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations without call or prepayment penalties.

	Available for Sale		Held to Maturity	
(In thousands)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Due in one year or less	$ 7,104	$ 7,155	$ 4,020	$ 4,020
Due after one year through five years	51,651	52,966	1,504	1,504
Due after five years through ten years	23,883	25,216	809	809
Due after ten years	2,000	2,039	1,225	1,225
Securities not due at a single maturity date	54,759	55,704	-	-
	$ 139,397	$ 143,080	$ 7,558	$ 7,558

During 2011, the Company sold $13.6 million of available for sale securities, while in 2010 the Company sold $35.6 million of available for sale securities. Gross gains on the sales/calls of investments in 2011 were $407,000. Gross gains on the sales/calls of investment securities in 2010 were $727,000. Investment securities with carrying amounts of $100.0 million and $76.2 million at December 31, 2011 and 2010, respectively, were pledged to secure deposits as required or permitted by law.

NOTE 4 - LOANS

Loans consist of the following at December 31, 2011 and 2010:

(In thousands)	2011	2010
Residential real estate:		
1-4 family	$ 91,883	$ 72,805
Home equity	51,800	48,168
Commercial	84,193	72,978
Agriculture	20,839	19,792
Total mortgage loans on real estate	248,715	213,743
Commercial loans	58,778	51,439
Agriculture loans	23,024	19,790
Consumer installment loans:		
Direct	14,413	12,916
Indirect	15,021	14,741
Total consumer installment loans	29,434	27,657
Total loans	$ 359,951	$ 312,629

Net unamortized loan origination costs totaled $677,000 and $385,000 at December 31, 2011 and 2010, respectively and are included with their related loan class.

NOTE 4 - LOANS (Continued)

The Company has transferred a portion of its originated commercial, commercial real estate, agriculture and agriculture real estate loans to participating lenders. The amounts transferred have been accounted for as sales and are therefore not included in the Company's accompanying consolidated balance sheets. The Company and participating lenders share ratably in cash flows and any gains or losses that may result from a borrower's lack of compliance with contractual terms of the loan. The Company continues to service the loans on behalf of the participating lenders and, as such, collects cash payments from the borrowers, remits payments (net of servicing fees) to participating lenders and disburses required escrow funds to relevant parties. At December 31, 2011 and 2010, the Company was servicing loans for participants aggregating $6.7 million and $9.0 million, respectively.

Loans are considered past due if the required principal and interest payments have not been received as of the date such payments are due. Generally loans are placed on nonaccrual status if principal or interest payments become 90 days or more past due and/or management deems the collectability of the principal and/or interest to be in question, as well as when required by regulatory requirements. The majority of the Company's loans classified as nonaccrual are not past due in accordance with their contractual obligations; however there are facts and circumstances regarding these loans that deem the collectability of the contractual payments to be in question.

The following table presents past due loans by classes of the loan portfolio at December 31, 2011 and 2010:

(In thousands)	Current	30-89 Days Past Due	90 Days and Greater	Total Loans	Loans on Nonaccrual
December 31, 2011:					
Residential real estate:					
1-4 family	$ 91,538	$ 231	$ 114	$ 91,883	$ 197
Home equity	51,392	408	-	51,800	-
Commercial real estate	83,817	376	-	84,193	4,956
Agriculture real estate	20,839	-	-	20,839	211
Commercial loans	58,600	178	-	58,778	371
Agriculture loans	23,018	6	-	23,024	6
Consumer installment loans:					
Direct	14,383	15	15	14,413	-
Indirect	14,981	40	-	15,021	200
Total	$ 358,568	$ 1,254	$ 129	$ 359,951	$ 5,941

(In thousands)	Current	30-89 Days Past Due	90 Days and Greater	Total Loans	Loans on Nonaccrual
December 31, 2010:					
Residential real estate:					
1-4 family	$ 72,805	$ -	$ -	$ 72,805	$ -
Home equity	48,084	84	-	48,168	-
Commercial real estate	72,110	428	440	72,978	4,435
Agriculture real estate	19,792	-	-	19,792	275
Commercial loans	50,924	256	259	51,439	623
Agriculture loans	19,777	13	-	19,790	1
Consumer installment loans:					
Direct	12,882	34	-	12,916	-
Indirect	14,477	264	-	14,741	267
Total	$ 310,851	$ 1,079	$ 699	$ 312,629	$ 5,601

At December 31, 2011 and 2010, loans that were over 90 days delinquent and still accruing totaled $15,000 and $0, respectively.

The changes in the allowance for loan losses are as follows for the years ended December 31, 2011 and 2010:

(In thousands)		**2011**		2010
Balance, January 1,	**$**	**6,441**	$	4,912
Provision for loan losses		**965**		2,405
Recoveries		**229**		124
Charge-offs		**(634)**		(1,000)
Balance, December 31,	**$**	**7,001**	$	6,441

Activity in the allowance for loan losses for the year ended December 31, 2011 follows:

(In thousands)	**Commercial**	**Commercial Real Estate**	**Agriculture**	**Agriculture Real Estate**	**Residential Real Estate**	**Consumer**	**Unallocated**	**Total**
December 31, 2011								
Beginning balance	$ 1,110	$ 2,040	$ 210	$ 152	$ 1,054	$ 517	$ 1,358	$ 6,441
Provisions for loan losses	346	720	49	15	400	(52)	(513)	965
Recoveries of loans previously charged off	62	10	-	-	19	138	-	229
Loans charged off	(308)	-	-	-	(111)	(215)	-	(634)
Ending balance	$ 1,210	$ 2,770	$ 259	$ 167	$ 1,362	$ 388	$ 845	$ 7,001

The allocation of the allowance for loan losses by loan type is as follows at December 31, 2011 and 2010:

(In thousands)	**Commercial**	**Commercial Real Estate**	**Agriculture**	**Agriculture Real Estate**	**Residential Real Estate**	**Consumer**	**Unallocated**	**Total**
December 31, 2011								
Amount of allowance for loan losses on loans individually evaluated for impairment	$ 124	$ 1,687	$ -	$ -	$ -	$ -	$ -	$ 1,811
Amount of allowance for loan losses on loans collectively evaluated for impairment	1,086	1,083	259	167	1,362	388	845	5,190
Total allowance for loan losses	$ 1,210	$ 2,770	$ 259	$ 167	$ 1,362	$ 388	$ 845	$ 7,001
Loans individually evaluated for impairment	$ 371	$ 4,956	$ 6	$ 211	$ -	$ -	$ -	$ 5,544
Loans collectively evaluated for impairment	58,407	79,237	23,018	20,628	143,683	29,434	-	354,407
Total Loans	**$ 58,778**	**$ 84,193**	**$ 23,024**	**$ 20,839**	**$ 143,683**	**$ 29,434**	**$ -**	**$ 359,951**
December 31, 2010								
Amount of allowance for loan losses on loans individually evaluated for impairment	$ 299	$ 824	$ -	$ -	$ -	$ -	$ -	$ 1,123
Amount of allowance for loan losses on loans collectively evaluated for impairment	811	1,216	210	152	1,054	517	1,358	5,318
Total allowance for loan losses	$ 1,110	$ 2,040	$ 210	$ 152	$ 1,054	$ 517	$ 1,358	$ 6,441
Loans individually evaluated for impairment	$ 623	$ 4,435	$ 1	$ 275	$ -	$ -	$ -	$ 5,334
Loans collectively evaluated for impairment	50,816	68,543	19,789	19,517	120,973	27,657	-	307,295
Total Loans	**$ 51,439**	**$ 72,978**	**$ 19,790**	**$ 19,792**	**$ 120,973**	**$ 27,657**	**$ -**	**$ 312,629**

NOTE 4 - LOANS (Continued)

Management is committed to early recognition of loan problems and to maintaining an adequate allowance. At least quarterly, management reviews all commercial and commercial real estate loans and leases and agriculturally related loans with an outstanding principal balance of over $100,000 that are internally risk rated special mention or worse, giving consideration to payment history, debt service payment capacity, collateral support, strength of guarantors, local market trends, industry trends, and other factors relevant to the particular borrowing relationship. Through this process, management identifies impaired loans. For loans considered impaired, estimated exposure amounts are based upon collateral values or present value of expected future cash flows discounted at the original effective interest rate of each loan. For commercial loans, commercial mortgage loans, agricultural mortgages and agricultural loans not specifically reviewed, and for homogenous loan portfolios such as residential mortgage loans and consumer loans, estimated exposure amounts are assigned based upon historical net loss experience and current charge-off trends, past due status, and management's judgment of the effects of current economic conditions on portfolio performance. In determining and assigning historical loss factors to the various homogeneous portfolios, the Company calculates average net losses over a period of time and compares this average to current levels and trends to ensure that the calculated average loss factor is reasonable.

Significant factors that could give rise to changes in these estimates may include, but are not limited to, changes in economic conditions in the local area, concentration of risk, changes in interest rates, and declines in local property values. While management uses available information to recognize losses on loans, future additions to the allowance may be necessary. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for loan losses. Such agencies may require the Company to recognize additions to the allowance based on their judgments about information available to them at the time of their examination.

The unallocated portion of the allowance for loan losses is maintained to cover uncertainties that could affect management's estimate of probable losses. The primary reason for the decrease in the unallocated portion of the allowance for loan losses year over year was in response to a review of the Company's largest impaired loan. During 2010, this relationship was deemed impaired and a specific allocation was determined using the information available to the Company. The relationship was subsequently restructured in the third quarter of 2010, and has since performed according to its contractual agreement. During 2011, a review of possible outcomes was performed relating to this significant relationship, to better quantify the impact to the Company if the loan discontinued making regular payments and became further distressed. As a result of that review, which included assumptions regarding collateral values in a variety of disposal situations, management allocated an additional $500,000 from the unallocated portion of the allowance as a specific allocation to this credit.

The above allocation is neither indicative of the specific amounts or the loan categories in which future charge-offs may occur, nor is it an indicator of future loss trends. The allocation of the allowance to each category does not restrict the use of the allowance to absorb losses in any category.

The following table summarizes information regarding impaired loans by loan portfolio class as of December 31, 2011 and 2010:

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2011					
With no related allowance recorded:					
Commercial loans	$ 247	$ 270	$ -	$ 72	$ 3
Commercial real estate	-	-	-	151	-
Agriculture loans	6	10	-	6	2
Agriculture real estate	211	377	-	231	-
With an allowance recorded:					
Commercial loans	124	124	124	245	-
Commercial real estate	4,956	5,327	1,687	4,887	-
Total	$ 5,544	$ 6,108	$ 1,811	$ 5,592	$ 5
Summary:					
Commercial	$ 5,327	$ 5,721	$ 1,811	$ 5,355	$ 3
Agriculture	217	387	-	237	2
Total	$ 5,544	$ 6,108	$ 1,811	$ 5,592	$ 5

(In thousands)	Recorded Investment	Unpaid Principal Balance	Related Allowance	Average Recorded Investment	Interest Income Recognized
December 31, 2010					
With no related allowance recorded:					
Commercial loans	$ 5	$ 8	$ -	$ 83	$ 16
Commercial real estate	440	850	-	1,752	1
Agriculture loans	1	24	-	121	6
Agriculture real estate	275	392	-	294	-
With an allowance recorded:					
Commercial loans	618	620	299	575	14
Commercial real estate	3,995	4,110	824	1,310	-
Agriculture loans	-	-	-	32	-
Total	$ 5,334	$ 6,004	$ 1,123	$ 4,167	$ 37
Summary:					
Commercial	$ 5,058	$ 5,588	$ 1,123	$ 3,720	$ 31
Agriculture	276	416	-	447	6
Total	$ 5,334	$ 6,004	$ 1,123	$ 4,167	$ 37

NOTE 4 - LOANS (Continued)

The following is a summary of troubled debt restructurings for the year ended December 31, 2011:

(In thousands)

	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Troubled debt restructurings:			
Commercial real estate	3	$ 4,070	$ 3,294

Two commercial real estate loans were granted an extension beyond normal circumstances to repay protective tax advances. The other commercial loan was granted a rate reduction. Management performs a discounted cash flow calculation to determine the amount of impairment reserves required on each of the troubled debt restructurings.

Any reserve required is recorded through the provision for loan losses. The TDRs identified in 2010 required impairment reserves of $824,000. There were no troubled debt restructurings that defaulted in the first twelve months after restructuring was granted.

Credit Quality

The Company utilizes a ten grade internal loan rating system for commercial, commercial real estate, agriculture and agriculture real estate loans. Loans that are rated “1” through “6” are considered “pass” rated loans with low to average risk.

Loans rated a “7” are considered “special mention”. These loans have potential weakness that deserves management’s close attention. These weaknesses may, if not checked or corrected, weaken the asset or inadequately protect the Company’s position at some future date. Borrowers may be experiencing adverse operating trends, or an ill-proportioned balance sheet. Adverse economic or market conditions may also support a special mention rating. These assets pose elevated risks, but their weakness does not yet justify a substandard classification.

Loans rated an “8” are considered “substandard”. Generally a loan is considered substandard if it is inadequately protected by the current net worth and paying capacity of the obligors and/or the collateral pledged. Substandard loans have a high probability of payment default or they have other well-defined weaknesses. They require more intensive supervision by Company management. Substandard loans are generally characterized by current or unexpected unprofitable operations, inadequate debt service coverage, inadequate liquidity, or marginal capitalization.

Loans rated a “9” are considered “doubtful”. Loans classified as doubtful have all the weaknesses inherent in those classified as substandard with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently existing facts, highly questionable and improbable. There were no doubtful loans at December 31, 2011 or 2010.

Loans rated a “10” are considered uncollectible (“loss”) and of such little value that their continuance as loans is not warranted. This classification does not mean that the loan has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this basically worthless loan even though partial recovery may be affected in the future. There were no loss loans at December 31, 2011 or 2010.

On an annual basis, or more often if needed, the Company formally reviews the ratings on all commercial, commercial real estate, agriculture and agriculture real estate loans. The Company also annually engages an independent third party to review a significant portion of loans within these segments. Management uses the results of these reviews as part of its annual review process.

Credit Quality (Continued)

The following table presents the classes of the commercial and agriculture loan portfolios summarized by the aggregate pass rating and the criticized and classified ratings of special mention and substandard within the Company's internal risk rating system as of December 31, 2011 and 2010:

(In thousands)	Commercial	Commercial Real Estate	Agriculture	Agriculture Real Estate	Total
December 31, 2011					
Grade:					
Pass	$ 51,970	$ 74,314	$ 21,732	$ 18,025	$ 166,041
Special Mention	5,245	1,259	19	62	6,585
Substandard	1,563	8,620	1,273	2,752	14,208
Total	**$ 58,778**	**$ 84,193**	**$ 23,024**	**$ 20,839**	**$ 186,834**
December 31, 2010					
Grade:					
Pass	$ 44,984	$ 61,324	$ 19,100	$ 18,093	$ 143,501
Special Mention	4,576	3,011	74	546	8,207
Substandard	1,879	8,643	616	1,153	12,291
Total	**$ 51,439**	**$ 72,978**	**$ 19,790**	**$ 19,792**	**$ 163,999**

Loans within the residential real estate and consumer portfolios do not have an internal loan rating system. Instead, they are monitored for past due status. If a residential real estate or consumer loan becomes 90 days past due, it is placed into nonaccrual status and the accrual of interest is discontinued.

Past due status is based on contractual terms of the loan. In all cases, loans are placed on nonaccrual if collection of principal or interest is considered doubtful.

The following table presents the classes of the residential real estate and consumer loan portfolios summarized by performing or nonaccrual as of December 31, 2011 and 2010:

(In thousands)	1-4 Family	Home Equity	Consumer - Direct	Consumer - Indirect	Total
December 31, 2011					
Performing	$ 91,686	$ 51,800	$ 14,413	$ 14,821	$ 172,720
Nonaccrual	197	-	-	200	397
Total	**$ 91,883**	**$ 51,800**	**$ 14,413**	**$ 15,021**	**$ 173,117**
December 31, 2010					
Performing	$ 72,805	$ 48,168	$ 12,916	$ 14,474	$ 148,363
Nonaccrual	-	-	-	267	267
Total	**$ 72,805**	**$ 48,168**	**$ 12,916**	**$ 14,741**	**$ 148,630**

NOTE 5 - LAND, PREMISES AND EQUIPMENT

Land, premises and equipment, net consist of the following at December 31, 2011 and 2010:

(In thousands)		**2011**		2010
Land	**$**	**2,956**	$	2,956
Buildings		**10,792**		10,397
Furniture and equipment		**5,482**		5,210
Leasehold improvements		**427**		427
Construction in progress		**1,332**		-
	$	**20,989**	$	18,990
Less accumulated depreciation		(6,293)		(5,634)
Total	**$**	**14,696**	$	13,356

Depreciation and amortization expense in 2011 and 2010 are included in noninterest expense as follows:

(In thousands)		**2011**		2010
Buildings	**$**	**277**	$	250
Furniture and equipment		**471**		435
Leasehold improvements		**8**		17
Total	**$**	**756**	$	702

As of December 31, 2011, the Bank had commitments of approximately $800,000 for additional capital expenditures.

At December 31, 2011, the Bank leased three of its branch facilities under non-cancelable operating leases. Future minimum rental payments under these leases are as follows:

Years Ending December 31,		*(In thousands)*
2012	$	101
2013		91
2014		44
2015		-
2016		-
Thereafter		-
Total	$	236

Rent expense under the operating leases totaled $117,000 and $114,000 in 2011 and 2010, respectively.

At December 31, 2011, the Bank leased out space under non-cancelable operating leases. Future minimum rental payments to be received by the Company under these leases are as follows:

Years Ending December 31,		*(In thousands)*
2012	$	129
2013		130
2014		132
2015		118
2016		87
Thereafter		387
Total	$	983

Rent income under the operating leases totaled $82,000 and $85,000 in 2011 and 2010, respectively.

NOTE 6 - DEPOSITS

Certificates of deposit in denominations of $100,000 and over were $55.3 million and $51.9 million at December 31, 2011 and 2010, respectively.

At December 31, 2011, scheduled maturities of time deposits are as follows:

Years Ending December 31,	*(In thousands)*
2012	$ 90,121
2013	16,707
2014	3,218
2015	2,160
2016	2,849
Total	$ 115,055

NOTE 7 - SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

Information concerning securities sold under agreements to repurchase as of and for the years ended December 31 is summarized as follows:

(In thousands)	**2011**	2010
Average balance	**$ 7,416**	$ 8,106
Maximum month-end balance	**$ 8,832**	$ 9,510
Carrying amounts of securities, including accrued interest, underlying the agreements	**$ 7,983**	$ 9,290

Securities sold under agreements to repurchase mature in less than 90 days from the transaction date. Securities sold under agreements to repurchase either remain under the control of the Bank or are held in third party custodial accounts that recognize the Bank's interest in the securities.

NOTE 8 - BORROWINGS

Borrowings consist of overnight advances and fixed rate term borrowings. At December 31, 2011 and 2010, there were $15.0 million and $25.8 million in overnight advances outstanding, respectively. The table below details additional information related to overnight advances for the years ended December 31,

(Dollars in thousands)	**2011**	2010
Average outstanding balance	**$ 6,190**	$ 6,800
Interest expense	**$ 23**	$ 31
Weighted average interest rate during the year	**0.37%**	0.45%
Weighted average interest rate at end of year	**0.31%**	0.40%

NOTE 8 - BORROWINGS (Continued)

At December 31, 2011 and 2010, there were term advances outstanding of $20.0 million and $11.0 million, respectively. During the year ended December 31, 2011, $6.0 million in term borrowings matured and were repaid. Term borrowings at December 31, 2011 consisted of $20.0 million of fixed rate, fixed term advances with a weighted average rate of 0.65% and a weighted average maturity of 4 months. Term borrowings at December 31, 2010 consisted of $11.0 million of fixed rate, fixed term advances with a weighted average rate of 1.61% and a weighed average maturity of 10 months.

Scheduled maturities for term borrowings at December 31, 2011 were as follows:

Years Ending December 31,		(In thousands)
2012	$	20,000
Total	$	20,000

As a member of the FHLB, the Bank can use certain unencumbered mortgage-related assets to secure borrowings from the FHLB. At December 31, 2011, total unencumbered mortgage-related loans were $25.7 million. Additional assets may also qualify as collateral for FHLB advances.

The Company, through the Bank, can use certain unencumbered collateral to secure borrowings at the Federal Reserve Bank. At December 31, 2011, total unencumbered collateral in the form of home equity loans and other consumer loans totaled $48.6 million.

The Company, through the Bank, had available unsecured line of credit agreements with correspondent banks permitting borrowings to a maximum of $10.0 million at December 31, 2011 and 2010. There were no outstanding advances against those lines at December 31, 2011 or 2010.

NOTE 9 - JUNIOR SUBORDINATED DEBENTURES

On June 27, 2003, the Company issued $1.035 million in junior subordinated debentures due June 27, 2033, to Trust I. The Company owns all of the $35,000 in common equity of Trust I and the debentures are the sole asset of Trust I. Trust I issued $1.0 million of floating-rate trust capital securities in a non-public offering. The floating-rate capital securities provide for quarterly distributions at a variable annual coupon rate, reset quarterly, based on three-month LIBOR plus 2.75%. The coupon rate was 3.330% at December 31, 2011, and 3.053% at December 31, 2010. The securities are callable by the Company, subject to any required regulatory approval, at par, after June 2008.

The Company unconditionally guarantees the Trust I capital securities. The terms of the junior subordinated debentures and the common equity of Trust I mirror the terms of the trust capital securities issued by Trust I. The Company used the net proceeds from this offering to fund an additional $1.0 million capital investment in the Bank to fund its operations and future growth.

On August 23, 2004, the Company issued $5.155 million in junior subordinated debentures due August 23, 2034, to Trust II. The Company owns all of the $155,000 in common equity of Trust II and the debentures are the sole asset of Trust II. Trust II issued

NOTE 9 - JUNIOR SUBORDINATED DEBENTURES (Continued)

$5.0 million of floating-rate trust capital securities in a non-public offering. The floating-rate capital securities provide for quarterly distributions at a variable annual coupon rate, reset quarterly, based on three-month LIBOR plus 2.65%. The coupon rate was 3.145% at December 31, 2011 and 2.934% at December 31, 2010. The securities are callable by the Company subject to any required regulatory approval, at par, after August 2009.

The Company unconditionally guarantees the Trust II capital securities. The terms of the junior subordinated debentures and the common equity of Trust II mirror the terms of the trust capital securities issued by Trust II. The Company used the net proceeds from this offering to fund an additional $5.0 million capital investment in the Bank to fund its operations and future growth.

In December 2009, the Company entered into an interest rate swap agreement (swap) with an effective date of February 23, 2011. The Company designated the swap as a cash flow hedge and it is intended to protect against the variability of cash flows associated with Trust II. The swap modifies the pricing characteristic of Trust II, wherein the Company receives interest at three-month LIBOR plus 2.65% from a counterparty and pays a fixed rate of interest of 6.80% to the same counterparty calculated on a notional amount of $5.0 million. This agreement will expire on November 23, 2019. The swap agreement was entered into with a counterparty that met the Company's credit standards, and the agreement contains collateral provisions protecting the at-risk party. The Company believes that the credit risk inherent in this contract is not significant. At December 31, 2011, the company pledged $1.0 million cash collateral to the counterparty.

At December 31, 2011 and 2010, the fair value of the swap agreement was a loss of $933,000 and $383,000, respectively, and was the amount the Company would have expected to pay to terminate the agreement. The fair value of the swap is included in other liabilities in the accompanying consolidated balance sheets. The net effect of the swap increased interest expense by $166,000 in 2011 and $0 in 2010.

On February 12, 2010, the Company issued $3.027 million in junior subordinated debentures due February 12, 2040, to Trust III. The Company owns all of the $95,000 in common equity of Trust III and the debentures are the sole asset of Trust III. Trust III issued $2.932 million of fixed rate convertible trust capital securities in a non-public offering. These capital securities provide for quarterly distributions at a fixed annual coupon rate of 6.00%. The securities are callable by the Company, subject to any required regulatory approval, at par, after February 2015. Holders of the trust securities may convert the securities, at any time, into shares of the Company's common stock at a conversion price of $27.78 per share, subject to adjustments for splits, stock dividends, recapilization and the like and issuances on a pro rata basis below the current market value, in-kind dividends and tender offers above market value.

The Company unconditionally guarantees the Trust III capital securities. The terms of the junior subordinated debentures and the common equity of Trust III mirror the terms of the convertible trust capital securities issued by Trust III. The Company used the net proceeds from this offering to fund an additional $2.9 million capital investment in the Bank for its operations and future growth.

In accordance with ASC Topic 810, Consolidation, the accounts of Trust I, Trust II and Trust III are not included in the consolidated financial statements of the Company. However, for regulatory purposes, the trust capital securities qualify as Tier I capital of the Company subject to a 25% of capital limitation under risk-based capital guidelines. The portion that exceeds the 25% of capital limitation qualifies as Tier II capital. At December 31, 2011 and 2010, $9.0 million in trust capital securities qualified as Tier I capital.

NOTE 10 - INCOME TAXES

The provision for income taxes consists of the following for the years ended December 31:

(In thousands)		**2011**		2010
Current tax provision:				
Federal	**$**	**1,759**	$	1,726
State		**1**		1
Total current tax provision		**1,760**		1,727
Deferred tax expense/(benefit):				
Federal	**$**	**(71)**	$	(233)
State		**71**		(10)
Total deferred tax expense/(benefit)		**-**		(243)
Total	**$**	**1,760**	$	1,484

The provision for income taxes differs from that computed by applying statutory rates to income before income taxes primarily due to the effects of tax exempt income from investment securities and bank owned life insurance.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes. Components of the Company's net deferred tax assets at December 31, included in other assets in the accompanying consolidated balance sheets, are as follows:

(In thousands)		**2011**		2010
Deferred tax assets:				
Allowance for loan losses	**$**	**2,559**	$	2,290
Compensation and benefits		**2,870**		1,865
Other		**458**		375
Total deferred tax assets	**$**	**5,887**	$	4,530
Deferred tax liabilities:				
Prepaid pension	**$**	**1,009**	$	943
Depreciation		**645**		573
Net unrealized gains on available for sale securities		**1,473**		200
Other		**557**		385
Total deferred tax liabilities	**$**	**3,684**	$	2,101
Net deferred tax assets	**$**	**2,203**	$	2,429

Management believes it is more likely than not that all of the deferred tax assets will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced.

At December 31, 2011 and December 31, 2010, the Company had no unrecognized tax benefits. The Company does not expect the total amount of unrecognized tax benefits to significantly increase within the next twelve months. The Company recognizes interest and penalties on unrecognized tax benefits in income tax expense in its Consolidated Statements of Income.

The Company conducts business only within New York State, and therefore files only federal and New York State tax returns. As the Company does not take uncertain tax positions, it has established no liability for uncertain tax positions. The Company did not have any accrued interest or penalties associated with any unrecognized tax benefits.

In the normal course of business the Company is subject to examination by taxing authorities. The Company is no longer subject to U.S. federal or state income tax examinations for years before 2007.

NOTE 11 - STOCKHOLDERS' EQUITY

The common stock and treasury stock of the Company at December 31, 2011 and 2010 are as follows:

	2011	2010
Common stock, authorized shares, $0.50 par value	**2,000,000**	2,000,000
Issued shares(1)	**1,301,496**	1,301,496
Less: treasury stock shares(1)	**(11,618)**	(14,527)
Outstanding shares(1)	**1,289,878**	1,286,969

(1) Per share amounts have been adjusted to reflect a 3-for-2 stock split, effective February 29, 2012.

Total comprehensive income is reported in the accompanying consolidated statements of stockholders' equity.

Information related to net other comprehensive income (loss) is as follows:

(In thousands)	**2011**	2010
Other comprehensive income (loss):		
Securities available for sale:		
Changes in net unrealized gains during the year	**$ 3,591**	$ (160)
Reclassification adjustment for gains included in income	**(407)**	(727)
Pension and postretirement benefits:		
Amortization of prior service costs	**1**	1
Amortization of net loss	**104**	89
Net actuarial loss	**(2,175)**	(423)
Change in net unrealized losses on the effective portion of cash flow hedge	**(550)**	(515)
	564	(1,735)
Tax (liability) benefit	**(225)**	694
Total other comprehensive income (loss)	**$ 339**	$ (1,041)

The components of accumulated other comprehensive loss, net of tax, as of December 31 were as follows:

(In thousands)	**2011**	2010
Net actuarial losses and prior service costs for pension and postretirement benefit plans	**$ (2,432)**	$ (1,190)
Net unrealized gain on securities available for sale	**2,209**	299
Net unrealized loss on the effective portion of cash flow hedge	**(559)**	(230)
Accumulated other comprehensive loss	**$ (782)**	$ (1,121)

NOTE 12 - PENSION AND POSTRETIREMENT BENEFIT PLANS

The Company participates in the New York State Bankers Retirement System (the "System"), a non-contributory defined benefit pension plan (the "Pension Plan") covering substantially all employees. The benefits are based on years of service and the employee's highest average compensation during five consecutive years of employment.

The Company also maintains an unfunded postretirement health insurance plan (the "Healthcare Plan") for certain employees meeting eligibility requirements.

The Company engages independent, external actuaries to compute the amounts of liabilities and expense relating to these plans, subject to the assumptions that the Company selects. The benefit obligation for these plans represents the liability of the Company for current and retired employees, and is affected primarily by the following: service cost (benefits attributed to employee service during the period); interest cost (interest on the liability due to the passage of time); actuarial gains/losses (experience during the year different from that assumed and changes in plan assumptions); and benefits paid to participants.

The following table provides a reconciliation of the changes in the Pension Plan's benefit obligations and fair value of assets and the accumulated benefit obligation for the Healthcare Plan for the years ending December 31, 2011 and 2010:

	Pension Plan		Healthcare Plan	
(In thousands)	**2011**	2010	**2011**	2010
Change in benefit obligation:				
Benefit obligation at beginning of year	**$ 5,574**	$ 4,519	**$ 388**	$ 396
Service cost	**599**	481	**4**	3
Interest cost	**296**	262	**24**	25
Actuarial loss (gain)	**1,719**	510	**38**	(6)
Expenses	**(7)**	(3)	**-**	-
Benefits paid	**(216)**	(195)	**(30)**	(30)
Benefit obligation at end of year	**7,965**	**5,574**	**424**	**388**
Change in benefit obligation:				
Fair value of plan assets at beginning of year	**6,065**	$ 4,662	**-**	-
Actual return on plan assets	**1**	398	**-**	-
Employer contribution	**750**	1,200	**30**	30
Benefits paid	**(216)**	(195)	**(30)**	(30)
Fair value of plan assets at end of year	**6,600**	6,065	**-**	-
Funded status recognized	**$ (1,365)**	$ 491	**$ (424)**	$ (388)
Accumulated benefit obligation	**$ 6,380**	$ 4,630	**$ 424**	$ 388

The underfunded status of the Pension Plan has been recognized in other liabilities in the consolidated balance sheet at December 31, 2011 and the overfunded status was recognized in other assets in the consolidated balance sheet as of December 31, 2010. The unfunded status of the Healthcare Plan has been recognized in other liabilities as of December 31, 2011 and 2010.

The components of net periodic benefit cost and other comprehensive income are as follows:

	Pension Plan		Healthcare Plan	
(In thousands)	**2011**	2010	**2011**	2010
Components of net periodic benefit cost:				
Service cost	**$ 599**	$ 481	**$ 4**	$ 3
Interest cost	**296**	262	**24**	25
Expected return on plan assets	**(417)**	(322)	**-**	-
Amortization of prior service cost	**1**	1	**-**	-
Amortization of net loss	**100**	85	**4**	4
Net periodic benefit cost	**$ 579**	**507**	**$ 32**	$ 32
Other changes in plan assets and benefit obligations recognized in other comprehensive income:				
Net loss (gain)	**$ 2,137**	$ 430	**$ 38**	$ (6)
Recognized actuarial loss	**(100)**	(85)	**(4)**	(4)
Recognized prior service cost	**(1)**	(1)	**-**	-
Recognized in other comprehensive income	**$ 2,036**	$ 344	**$ 34**	$ (10)
Total recognized in net periodic benefit cost and other comprehensive income	**$ 2,615**	$ 851	**$ 66**	$ 22

The following table presents the components of accumulated other comprehensive loss, net of taxes, as of December 31:

	Pension Plan		Healthcare Plan	
(In thousands)	**2011**	2010	**2011**	2010
Prior service cost (credit)	**$ 3**	$ 4	**$ (22)**	$ (28)
Net actuarial loss	**2,381**	1,164	**70**	50
Net periodic benefit cost	**$ 2,384**	$ 1,168	**$ 48**	$ 22

The estimated costs that will be amortized from accumulated other comprehensive loss into net periodic cost during 2012 are as follows:

(In thousands)	**Pension Plan**	**Healthcare Plan**	**Total**
Prior service cost (credit)	**$** 1	**$** (4)	$ (3)
Net actuarial loss	243	7	250
Total	**$ 244**	**$ 3**	$ 247

NOTE 12 - PENSION AND POSTRETIREMENT BENEFIT PLANS (Continued)

Weighted-average assumptions used in accounting for the plans were as follows:

	Pension Plan		Healthcare Plan	
	2011	2010	**2011**	2010
Discount rates:				
Benefit cost for Plan Year	**5.38%**	5.89%	**5.50%**	6.00%
Benefit obligation at end of Plan Year	**4.27%**	5.38%	**4.50%**	5.50%
Expected long-term return on plan assets	**7.00%**	7.00%	**N/A**	N/A
Rate of compensation increase:				
Benefit cost for Plan Year	**3.00%**	3.00%	**N/A**	N/A
Benefit obligation at end of Plan Year	**3.00%**	3.00%	**N/A**	N/A

The assumed health care cost trend rate used in the postretirement benefit plan at December 31, 2011 was 4.00%. Assumed health care trend rates may have a significant effect on the amounts reported for this plan. A 1% increase in the trend rate would increase the periodic benefit cost by $3,000 and increase the accumulated postretirement benefit obligation by $48,000.

The discount rate used for each period was based upon the rates of return on high-quality fixed income investments. The objective of using this approach is to measure the single amount that, if invested at the measurement date in a portfolio of high-quality debt instruments, would provide the necessary future cash flows to pay benefits when they became due. The discount rates are evaluated at each measurement date to give effect to changes in the general level of interest rates.

The Company's funding policy is to contribute, at a minimum, an actuarially determined amount that will satisfy the minimum funding requirements determined under the appropriate sections of the Internal Revenue Code. While the Company has satisfied the minimum funding requirement for 2011, it expects to contribute to the Pension Plan during 2012. However, the amount of the contribution is not known at this time.

Estimated future benefit payments, which reflect expected future service, as appropriate, are as follows:

	Pension Plan	Healthcare Plan
Years Ending December 31,	*(In thousands)*	
2012	$ 209	$ 32
2013	231	32
2014	262	32
2015	298	31
2016	327	31
2017 - 2021	2,107	151

The fair value of the Company's pension plan assets at December 31, 2011 and 2010 by asset category are as follows:

(In thousands)	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
December 31, 2011:				
Cash equivalents:				
Foreign currencies	**$ 12**	**$ 12**	**$ -**	**$ -**
Short term investment funds	**689**	**-**	**689**	
Total cash equivalents	**701**	**12**	**689**	**-**
Equity securities:				
U.S. large cap	**1,967**	**1,967**	**-**	**-**
U.S. mid cap	**268**	**268**	**-**	**-**
U.S. small cap	**6**	**6**	**-**	**-**
International	**921**	**921**	**-**	**-**
Total equity securities	**3,162**	**3,162**	**-**	**-**
Fixed income securities:				
Corporate bonds rated A or higher	**274**	**-**	**274**	**-**
Corporate bonds rated below A	**321**	**-**	**321**	**-**
Government issues	**1,497**	**-**	**1,497**	**-**
CMOs rated A or higher	**595**	**-**	**595**	**-**
CMOs rated below A	**50**	**-**	**50**	**-**
Total fixed income securities	**2,737**	**-**	**2,737**	**-**
Total	**$ 6,600**	**$ 3,174**	**$ 3,426**	**$ -**

(In thousands)	Total	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
December 31, 2010:				
Cash equivalents:				
Foreign currencies	$ 13	$ 13	$ -	$ -
Short term investment funds	668	-	668	
Total cash equivalents	681	13	668	-
Equity securities:				
U.S. large cap	1,691	1,691	-	-
U.S. mid cap	173	173	-	-
U.S. small cap	13	13	-	-
International	1,049	1,049	-	-
Total equity securities	2,926	2,926	-	-
Fixed income securities:				
Corporate bonds rated A or higher	331	-	331	-
Corporate bonds rated below A	232	-	232	-
Government issues	1,763	-	1,763	-
CMOs rated A or higher	91	-	91	-
CMOs rated below A	41	-	41	-
Total fixed income securities	2,458	-	2,458	-
Total	$ 6,065	$ 2,939	$ 3,126	$ -

Fair value is defined under ASC 820 "Fair Value Measurements and Disclosures" as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date.

NOTE 12 - PENSION AND POSTRETIREMENT BENEFIT PLANS (Continued)

Valuation techniques used to measure fair value under ASC 820 must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value which are the following:

- **Level 1**— Quoted prices in active markets for identical assets or liabilities.
- **Level 2**— Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- **Level 3**— Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

In instances in which the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input that is significant to the fair value measurement in its entirety. Investments valued using the NAV (Net Asset Value) are classified as Level 2 if the System can redeem its investment with the investee at the NAV at the measurement date. If the System can never redeem the investment with the investee at the NAV, it is considered a Level 3. If the System can redeem the investment at the NAV at a future date, the System's assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset.

There were no transfers in or out of Level 3 in the years ended December 31, 2011 and 2010.

The Pension Plan was established in 1938 to provide for the payment of benefits to employees of participating banks. The Pension Plan is overseen by a Board of Trustees who meet quarterly and set the investment policy guidelines.

The overall investment strategy is to achieve a mix of approximately 97% of investments for long-term growth and 3% for near-term benefit payments with a wide diversification of asset types, fund strategies, and fund managers. The target allocations are shown in the table below. Cash equivalents consist primarily of short term investment funds and foreign currencies. Equity securities primarily include investments in United States large, mid and small cap equity securities, as well as international equity securities. Fixed income securities include corporate bonds, government issued and mortgage backed securities.

The weighted average expected long-term rate of return is estimated based on current trends as well as projected future rates of return on those assets and reasonable actuarial assumptions based on the guidance provided by Actuarial Standard Of Practice No. 27 "Selection of Economic Assumptions for Measuring Pension Obligations" for long term inflation, and the real and nominal rate of investment return for a specific mix of asset classes. The following assumptions were used in determining the long-term rate of return:

Equity securities: Dividend discount model, the smoothed earnings yield model, and the equity risk premium model

Fixed income securities: Current yield-to-maturity and forecasts of future yields

The long term rate of return considers historical returns. Adjustments were made to historical returns in order to reflect expectations of future returns. These adjustments were due to factor forecasts by economists and long-term U.S. Treasury yields to forecast long-term inflation. In addition, forecasts by economists and others for long-term gross domestic product growth were factored into the development of assumptions for earnings growth and per capita income.

Effective September 2011, the investment guidelines were revised. Currently, investment managers are prohibited from purchasing the following investments:

Equity securities:

- Short sales,
- Unregistered securities, and
- Margin purchases.

Fixed income securities:

- Mortgage backed securities that have an inverse floating rate coupon or that are interest only securities,
- Any asset backed security that is not issued by the U.S. government or its agencies or instrumentalities,
- In general, securities of less than Baa2/BBB quality, and
- Securities of less than A-quality may not in the aggregate exceed 10% of the investment manager's portfolio.

Other financial instruments:

- Unhedged currency exposure in countries not defined as "high income economies" by the World Bank.

Prior to September 2011, investments in emerging countries as defined by the Morgan Stanley Emerging Markets Index and structured notes were prohibited.

All other investments not prohibited by policy are permitted. At December 31, 2011 the Pension Plan holds certain investments which are no longer deemed acceptable to acquire. These positions will be liquidated when the investment managers deem that such liquidation is in the best interest of the Pension Plan.

The target allocation for 2012 and actual allocation of plan assets as of December 31, 2011 and 2010 are as follows:

		% of Plan Assets at December 31,	
Asset Category	**Target Allocation 2012**	**2011**	**2010**
Cash equivalents	**0-20%**	**10.6%**	11.2%
Equity securities	**40-60%**	**47.9%**	48.2%
Fixed income securities	**40-60%**	**41.5%**	40.6%
Other financial instruments	**0-5%**	**-**	-

Defined Contribution Plan

The Bank has a contributory 401(k) Plan for substantially all employees. Employees are eligible to contribute a percentage of their salary up to the maximum as determined by the Internal Revenue Service. The Bank is required to match 75% of the employees' contributions up to a maximum of 6% of the employees' salaries. The Bank contributed $230,000 and $217,000 under these provisions during 2011 and 2010, respectively.

NOTE 12 - PENSION AND POSTRETIREMENT BENEFIT PLANS (Continued)

Supplemental Employee Retirement Plans

The Company maintains supplemental employee retirement plans (the "SERP") for certain executives. All benefits provided under the SERP are unfunded and, as these executives retire, the Company will make payments to plan participants. The unfunded status of the SERP at December 31, 2011 and 2010 was $2.2 million and $1.8 million, respectively, and is recorded in other liabilities in the consolidated balance sheet. Compensation expense related to the SERP was $360,000 and $340,000 for the years ended December 31, 2011 and 2010, respectively.

Deferred Compensation Plans

Prior to 2007, the Company had entered into employment agreements with key executives. These employment agreements established deferred compensation plans whereby Company stock was awarded and vested each year. In 2007, the Company terminated the employment agreements and related deferred compensation plans and established new deferred compensation plans for key executives. The new plans require a vesting period of three years from the original date the executive entered the plan. Awarded shares from both the prior plan and the current plan are restricted from being sold until employment is terminated.

The Company obtains shares for the new deferred compensation plan either through open market purchases or from treasury shares. The amount of awarded shares is based on the amount earned by each executive under the deferred compensation plan. The executives are awarded a number of shares based on the amount of deferred compensation earned divided by the value of the shares. The value of the shares purchased on the open market is the price paid. The value of the shares from treasury is the average daily closing price of the stock for each day within the past quarter. Total deferred compensation shares were 33,379 and 30,153 at December 31, 2011 and 2010, respectively. Total shares awarded were 3,226 and 3,645 for 2011 and 2010, respectively, while total nonvested shares were 29 and 54 at December 31, 2011 and 2010, respectively. Compensation expense is recognized over the vesting period, and is based upon the total amount of the value of the shares awarded to each executive. Compensation expense related to these plans was approximately $103,000 and $105,000 for the years ended December 31, 2011 and 2010, respectively.

NOTE 13 - EARNINGS PER SHARE

The following table presents a reconciliation of the earnings and shares used in calculating basic and diluted EPS for each of the years ended December 31:

(In thousands, except per share data)	**2011**	2010
Net income available to common shareholders	**$ 5,138**	$ 4,168
Adjustment for dilutive potential common shares	**107**	-
Net income available for diluted common shares	**$ 5,245**	$ 4,168
Weighted average common shares used to calculate basic EPS	**1,289,790**	1,287,225
Add: effect of common stock equivalents	**105,552**	-
Weighted average common shares used to calculate diluted EPS	**1,395,342**	1,287,225
Earnings per common share:		
Basic	**$ 3.98**	$ 3.24
Diluted	**$ 3.76**	$ 3.24

NOTE 14 - RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank has and expects to continue to have transactions, including loans and deposit accounts, with the Company's and the Bank's executive officers and directors and their affiliates. In the opinion of management, such transactions were on substantially the same terms, including interest rates and collateral, as those prevailing at the time of comparable transactions with other unrelated persons and did not involve more than a normal risk of collectability or present any other unfavorable features.

The rollforward of loans to related parties for the years ended December 31 is as follows:

(In thousands)	**2011**	2010
Beginning balance, January 1	**$ 9,211**	$ 9,606
New loans	**894**	965
Existing loans to new directors	**-**	567
Repayments	**(929)**	(1,927)
	9,176	9,211
Less loans to directors who retired during the year	**(3,398)**	-
Ending balance, December 31	**$ 5,778**	$ 9,211

The Bank has an operating lease with one of its directors. Under the terms of the lease, the Bank receives monthly payments of approximately $3,850 through August 2012, increasing 2.5% per year thereafter until August 2015.

NOTE 15 - COMMITMENTS AND CONTINGENT LIABILITIES

The Bank is a party to financial instruments with off-balance-sheet risk in the normal course of business to meet the financing needs of its customers. These financial instruments include commitments to extend credit and standby letters of credit. These instruments involve, to varying degrees, elements of credit and interest rate risk in excess of the amounts recognized in the consolidated balance sheets. The Bank uses the same credit policies in making commitments and conditional obligations as it does for on-balance-sheet instruments.

The Bank's exposure to credit loss in the event of nonperformance by the other party to the financial instrument for commitments to extend credit and standby letters of credit is represented by the contractual notional amount of those instruments summarized as follows at December 31:

(In thousands)	**2011**	2010
Commitments to extend credit:		
Commitments to grant loans	**$ 45,191**	$ 32,959
Unfunded commitments under commercial lines of credit	**38,006**	35,878
Unfunded commitments under consumer lines of credit	**34,078**	32,714
Standby letters of credit	**8,061**	6,384
	$ 125,336	$ 107,935

NOTE 15 - COMMITMENTS AND CONTINGENT LIABILITIES (Continued)

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements.

The Bank evaluates each customer's credit worthiness on a case-by-case basis. The amount and type of collateral obtained, if deemed necessary by the Bank upon extension of credit, varies and is based on management's credit evaluation of the counterparty.

Standby letters of credit are conditional lending commitments issued by the Bank to guarantee the performance of a customer to a third party. These letters of credit are primarily issued to support public and private borrowing arrangements. Generally, letters of credit issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers. The Bank's policy for obtaining collateral, and the nature of such collateral, is essentially the same as that involved in making commitments to extend credit. The Bank generally holds collateral supporting those commitments. Such collateral amounted to $7.8 million and $6.2 million at December 31, 2011 and 2010, respectively. The amount of the liability related to guarantees under standby letters of credit was not material at December 31, 2011 and 2010.

In addition to other investors, the Bank sells residential mortgage loans to the FHLB. The agreement with the FHLB includes a maximum credit enhancement liability of $3.3 million and $675,000 at December 31, 2011 and 2010, respectively, which the Bank may be required to pay if realized losses on any of the sold mortgages exceed the amount held in the FHLB's spread account. The FHLB is funding the spread account annually based on the outstanding balance of loans sold. The Bank's historical losses on residential mortgages have been lower than the amount being funded to the spread account. As such, the Bank does not anticipate recognizing any losses and, accordingly, has not recorded a liability for the credit enhancement.

NOTE 16 - CONCENTRATIONS OF CREDIT

The Company's loan customers are located primarily in the New York communities served by the Bank. Investments in state and local government securities also involve governmental entities within the Company's market area. Although operating in numerous communities in New York State, the Company is still dependant on the general economic conditions of New York. The largest concentration of credit by industry is Dairy Cattle and Milk Production, with loans outstanding of $14.8 million or 4.1% of total loans as of December 31, 2011. Risk related to this concentration is controlled through adherence to Farm Services Agency (FSA) standards for guaranteed loans, such as diligence in farm visits and loan closings per conditional commitments issued by FSA. The Company, as a matter of policy, does not extend credit to any single borrower, or group of related borrowers, in excess of its legal lending limit. Further information on the Company's lending activities is provided in "Note 4 Loans" in Notes to Consolidated Financial Statements.

NOTE 17 - REGULATORY MATTERS

The supervision and regulation of financial and bank holding companies and their subsidiaries is intended primarily for the protection of depositors, the deposit insurance funds regulated by the Federal Deposit Insurance Corporation ("FDIC") and the banking system as a whole, and not for the protection of shareholders or creditors of bank holding companies. The various bank regulatory agencies have broad enforcement power over financial holding companies and banks, including the power to impose substantial fines, operational restrictions and other penalties for violations of laws and regulations and for safety and soundness considerations.

Capital

The Bank is subject to various regulatory capital requirements administered by federal banking agencies. Failure to meet minimum capital requirements can initiate certain mandatory, and possibly additional discretionary, actions by regulators that, if undertaken, could have a direct material effect on the Company's consolidated financial statements. Under capital adequacy guidelines and the regulatory framework for prompt corrective action, the Bank must meet specific capital guidelines that involve quantitative measures of their assets, liabilities, and certain off-balance-sheet items as calculated under regulatory accounting practices. The capital amounts and classification are also subject to qualitative judgments by the regulators about components, risk weightings, and other factors.

Quantitative measures established by regulation to ensure capital adequacy require the Bank to maintain minimum amounts and ratios (set forth in the table below) of total and Tier I capital (as defined by regulation) and of Tier I capital (as defined) to average assets (as defined).

Management believes, as of December 31, 2011, that the Bank meets all capital adequacy requirements to which they are subject.
As of the most recent notification from the Office of the Comptroller of the Currency, the Bank was categorized as well capitalized. There are no conditions or events since the notification that management believes have changed the institution's category.

The Bank's capital amounts and ratios are also presented in the table below.

(Dollars In thousands)	**Actual**		**For Capital Adequacy Purposes**		**To be Well Capitalized under Prompt Corrective Action Provisions**	
	Amount	**Ratio**	**Amount**	**Ratio**	**Amount**	**Ratio**
December 31, 2011:						
Total risk-based capital	**$ 50,364**	**13.8 %**	**$ ≥ 29,107**	**≥ 8.0 %**	**$ ≥ 36,384**	**≥ 10.0 %**
Tier 1 capital	**$ 45,816**	**12.6 %**	**$ ≥ 14,554**	**≥ 4.0 %**	**$ ≥ 21,830**	**≥ 6.0 %**
Tier 1 leverage	**$ 45,816**	**8.4 %**	**$ ≥ 21,765**	**≥ 4.0 %**	**$ ≥ 27,206**	**≥ 5.0 %**
December 31, 2010:						
Total risk-based capital	$ 46,018	14.2 %	$ ≥ 25,948	≥ 8.0 %	$ ≥ 32,435	≥ 10.0 %
Tier 1 capital	$ 41,964	12.9 %	$ ≥ 12,974	≥ 4.0 %	$ ≥ 19,461	≥ 6.0 %
Tier 1 leverage	$ 41,964	8.2 %	$ ≥ 20,422	≥ 4.0 %	$ ≥ 25,528	≥ 5.0 %

Dividend Restrictions

In the ordinary course of business, the Company is dependent upon dividends from the Bank to provide funds for the payment of interest expense on the junior subordinated debentures, dividends to shareholders and to provide for other cash requirements. Banking regulations may limit the amount of dividends that may be paid. Approval by regulatory authorities is required if the effect of dividends declared would cause the regulatory capital of the Bank to fall below specified minimum levels. Approval is also required if dividends declared exceed the net profits for that year combined with the retained net profits for the preceding two years.

At December 31, 2011, the Bank's retained earnings available for the payment of dividends was approximately $11.8 million.

NOTE 18 - FAIR VALUE MEASUREMENTS AND FAIR VALUES OF FINANCIAL INSTRUMENTS

Determination of Fair Value

The Company uses fair value measurements to record fair value adjustments to certain assets and liabilities and to determine fair value disclosures. In accordance with the Fair Value Measurements and Disclosures topic of FASB ASC, the fair value of a financial instrument is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is best determined based upon quoted market prices. However, in many instances, there are no quoted market prices for the Company's various financial instruments. In cases where quoted market prices are not available, fair values are based on estimates using present value or other valuation techniques. Those techniques are significantly affected by the assumptions used, including the discount rate and estimates of future cash flows. Accordingly, the fair value estimates may not be realized in an immediate settlement of the instrument.

Fair value guidance provides a consistent definition of fair value, which focuses on exit price in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions. If there has been a significant decrease in the volume and level of activity for the asset or liability, a change in valuation technique or the use of multiple valuation techniques may be appropriate. In such instances, determining the price at which willing market participants would transact at the measurement date under current market conditions depends on the facts and circumstances and requires the use of significant judgment.

Fair Value Hierarchy

In accordance with this guidance, the Company groups its financial assets and financial liabilities generally measured at fair value in three levels, based on the markets in which the assets and liabilities are traded and the reliability of the assumptions used to determine fair value.

Level 1: Valuation is based on unadjusted quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. Level 1 assets and liabilities generally include debt and equity securities that are traded in an active exchange market.

Level 2: Valuation is based upon inputs other than quoted prices included within level 1 that are observable either directly or indirectly. The valuation may be based on quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liability.

Level 3: Valuation is based on unobservable inputs that are supported by little or no market activity and that are significant to the fair value measurement. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which determination of fair value requires significant management judgment or estimation.

An asset's or liability's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

The following information should not be interpreted as an estimate of the fair value of the entire Company since a fair value calculation is only provided for a limited portion of the Company's assets and liabilities. Due to a wide range of valuation techniques and the degree of subjectivity used in making the estimates, comparisons between the Company's disclosures and those of other companies may not be meaningful. The following methods and assumptions were used to estimate the fair values of the Company's financial instruments at December 31, 2011 and 2010:

Cash, Due From Banks, and Interest-bearing Deposits in Banks

The carrying amounts reported in the consolidated balance sheets for these assets approximate those assets' fair values based on the short-term nature of the assets.

Fair Value Hierarchy (Continued)

Investment Securities

The fair value of securities available for sale and held to maturity are determined by obtaining quoted market prices on nationally recognized securities exchanges (Level 1), or matrix pricing (Level 2), which is a mathematical technique used widely in the industry to value debt securities without relying exclusively on quoted market prices for the specific securities but rather by relying on the securities' relationship to other benchmark quoted prices. For certain securities which are not traded in active markets or are subject to transfer restrictions, valuations are adjusted to reflect illiquidity and/or non-transferability, and such adjustments are generally based on available market evidence (Level 3). In the absence of such evidence, management's best estimate is used. Management's best estimate consists of external support on certain Level 3 investments. Management has determined that the fair value of local government securities in the held to maturity portfolio approximate their carrying value. Restricted equity securities have restrictions on their sale and are carried at cost due to their limited marketability.

Loans Held for Sale

The fair value of loans held for sale is determined using quoted secondary-market prices. If no such quoted prices exist, the fair value of a loan is determined using quoted prices for a similar loan or loans, adjusted for the specific attributes of that loan.

Loans

The fair values of loans are estimated using discounted cash flow analysis, using market rates at the balance sheet date that reflect the credit and interest rate-risk inherent in the loans. Projected future cash flows are calculated based upon contractual maturity or call dates, projected repayments and prepayments of principal. Generally, for variable rate loans that reprice frequently and with no significant change in credit risk, fair values are based on carrying values.

Impaired Loans

The fair value of loans considered impaired is generally determined based upon independent third party appraisals of the properties, or discounted cash flows based upon the expected proceeds. These assets are included as Level 3 fair values, based upon the lowest level of input that is significant to the fair value measurements. The fair value consists of the loan balances of $5.1 million and $4.6 million, net of valuation allowances of $1.8 million and $1.1 million as of December 31, 2011 and 2010, respectively.

Accrued Interest Receivable and Payable

The carrying amount of accrued interest receivable and accrued interest payable approximates its fair value.

Mortgage Servicing Rights

The carrying amount of mortgage servicing rights approximates their fair value.

Deposits

The fair values disclosed for demand and savings deposits are, by definition, equal to the amount payable on demand at the reporting date (that is, their carrying amounts). Fair values for fixed-rate certificates of deposit are estimated using a discounted cash flow calculation that applies market interest rates on comparable instruments to a schedule of aggregated expected monthly maturities on time deposits.

Securities Sold Under Agreements to Repurchase

The carrying amounts of securities sold under agreements to repurchase approximate their fair values.

NOTE 18 - FAIR VALUE MEASUREMENTS AND FAIR VALUES OF FINANCIAL INSTRUMENTS (Continued)

Fair Value Hierarchy (Continued)

Borrowings from the Federal Home Loan Bank

Fair values of borrowings from the FHLB are estimated using discounted cash flow analysis, based on quoted prices for new borrowings from the FHLB with similar credit risk characteristics, terms and remaining maturity. These prices obtained from this active market represent a market value that is deemed to represent the transfer price if the liability were assumed by a third party.

Junior Subordinated Debentures

The fair values of junior subordinated debentures are estimated using discounted cash flow analysis, based on market rates currently offered on such debt with similar credit risk characteristics, terms and remaining maturity.

Interest Rate Swap Agreements

The fair values for interest rate swap agreements are based upon the amounts required to settle the contracts, which includes credit risk.

Off-Balance Sheet Financial Instruments

Fair values for off-balance sheet financial instruments (lending commitments and letters of credit) are based on fees currently charged in the market to enter into similar agreements, taking into account, the remaining terms of the agreements and the counterparties' credit standing.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

For financial assets measured at fair value on a recurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2011 and 2010 are as follows:

(In thousands)	**Carrying Value**	**(Level 1) Quoted Prices in Active Markets for Identical Assets**	**(Level 2) Significant Other Observable Inputs**	**(Level 3) Significant Unobservable Inputs**
December 31, 2011:				
Securities available for sale:				
United States treasuries	**$ 5,155**	**$ -**	**$ 5,155**	**$ -**
United States agencies	**30,812**	**-**	**30,812**	**-**
State and local governments	**51,409**	**-**	**51,409**	**-**
Mortgage-backed securities	**55,704**	**-**	**55,704**	**-**
Total securities available for sale	**$ 143,080**	**$ -**	**$ 143,080**	**$ -**
Interest rate swap agreements	**$ (933)**	**$ -**	**$ -**	**$ (933)**
December 31, 2010:				
Securities available for sale:				
United States treasuries	$ 12,977	$ -	$ 12,977	$ -
United States agencies	27,016	-	27,016	-
State and local governments	53,290	-	53,290	-
Mortgage-backed securities	61,013	-	61,013	-
Total securities available for sale	$ 154,296	$ -	$ 154,296	$ -
Interest rate swap agreements	$ (383)	$ -	$ -	$ (383)

Assets and Liabilities Measured at Fair Value on a Recurring Basis (Continued)

The following table presents a reconciliation of financial assets measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the year ended December 31:

(In thousands)	2011	2010
Beginning balance, January 1	**$ (383)**	$ 259
Principal payments	**-**	(127)
Unrealized loss included in other comprehensive income	**(550)**	(515)
Ending balance, December 31	**$ (933)**	$ (383)

Assets Measured at Fair Value on a Nonrecurring Basis

For financial assets measured at fair value on a nonrecurring basis, the fair value measurements by level within the fair value hierarchy used at December 31, 2011 and 2010 are as follows:

(In thousands)	Carrying Value	(Level 1) Quoted Prices in Active Markets for Identical Assets	(Level 2) Significant Other Observable Inputs	(Level 3) Significant Unobservable Inputs
December 31, 2011:				
Impaired loans	**$ 3,269**	**$ -**	**$ -**	**$ 3,269**
December 31, 2010:				
Impaired loans	$ 3,490	$ -	$ -	$ 3,490

The carrying amounts and estimated fair values of the Company's financial instruments at December 31, 2011 and 2010 are as follows:

(In thousands)	2011		2010	
	Carrying Amount	**Fair Value**	Carrying Amount	Fair Value
Financial assets:				
Cash and due from banks	**$ 13,749**	**$ 13,749**	$ 8,679	$ 8,679
Interest-bearing deposits in banks	**5,326**	**5,326**	7,000	7,000
Investment securities	**154,639**	**154,639**	162,551	162,551
Loans, net of allowance	**352,950**	**360,807**	306,188	309,802
Accrued interest receivable	**2,073**	**2,073**	2,025	2,025
Mortgage servicing rights	**462**	**462**	422	422
Financial liabilities:				
Deposits	**$ 460,099**	**$ 445,832**	$ 424,006	$ 424,431
Securities sold under agreements to repurchase	**7,058**	**7,058**	7,691	7,691
Borrowings from FHLB	**35,000**	**35,036**	36,800	36,881
Junior subordinated debentures	**9,217**	**8,263**	9,217	8,484
Interest rate swap agreements	**933**	**933**	383	383
Accrued interest payable	**93**	**93**	122	122

Amounts in the preceding table are included in the consolidated balance sheets under the applicable captions. The fair values of off-balance sheet financial instruments are not significant.

NOTE 19 - SUBSEQUENT EVENTS

The Company has evaluated events through the date these consolidated financial statements were available to be issued.

At a special meeting of the Company's shareholders held on February 15, 2012, the Company's shareholders (a) approved an amendment to the Company's Certificate of Incorporation that authorizes the increase of the Company's total number of authorized shares from 2,000,000 to 5,000,000 shares, with no change in the par value per share of $0.50, and (b) authorized a class of 5,000,000 liquidation value of convertible preferred stock.

At the February 16, 2012 board meeting, the Board of Directors approved a 3-for-2 stock split of the Company's common stock, effective February 29, 2012, for shareholders of record on February 28, 2012. All share data presented in the Company's financial statements has been adjusted retroactively to reflect this stock split.

At the February 28, 2012 board meeting, the Board of Directors approved a dividend of $0.30 per share, payable April 15, 2012, to shareholders of record on March 31, 2012.

Lyons Bancorp, Inc.
It's all about people.

PROFILE

Lyons Bancorp, Inc. is a bank holding company headquartered in Lyons, New York, with assets of $555.5 million at December 31, 2011. Lyons Bancorp, Inc. has one banking subsidiary, The Lyons National Bank.

The Lyons National Bank is a community bank with offices in Clyde, Lyons, Macedon, Newark, Ontario and Wolcott in Wayne County, Jordan in Onondaga County, Geneva in Ontario County, Penn Yan in Yates County and our newest office in Seneca County. The Lyons National Bank has one subsidiary, Lyons Realty Associates Corp.

STOCK SYMBOL

LYBC

BOARD OF DIRECTORS

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President & Chief Executive Officer
Lyons Bancorp, Inc. & The Lyons National Bank

David J. Breen, Jr.
General Manager
Herrema's Market Place

Clair J. Britt, Jr.
Executive Vice President & Senior Commercial Lending Officer
The Lyons National Bank

Joseph A. Fragnoli
Owner
Super Casuals

Andrew F. Fredericksen, CPA
Senior Partner
Fredericksen & Sirianni, LLP

Dale H. Hemminger
President & General Manager
Hemdale Farms & Greenhouses

James A. Homburger
Real Estate Broker

Thomas L. Kime
Executive Vice President & Chief Operating Officer
The Lyons National Bank

Brad A. Person
President & General Manager
Nuttall Golf Cars Inc. and Nuttall Golf Car Leasing, LLC

James E. Santelli
Retired Vice President & Co-owner
Santelli Lumber Co.

John J. Werner, Jr.
Retired President & Chief Executive Officer
Lyons Bancorp, Inc. & The Lyons National Bank

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